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DOCTORAL THESIS

Reforming Not-for-Profit Organisations in Australia : a Work in Progress

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Reforming Not-for-Profit Organisations in Australia: A Work in Progress.

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LLM (Research)

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2013

Certificate

This thesis is submitted to Bond University in fulfilment of the requirement for the Master of Laws research degree.

This thesis represents my own work and contains no material which has been previously submitted for a degree or diploma at this University or any other institution, except where due acknowledgement is made.

Signature:.....

Date:.....

Thesis Abstract

Reforming Not-for-Profit Organisations in Australia: A Work in Progress.

Incorporated associations are founded by, and subsequently operate exclusively on, the collective action of individuals, which is largely voluntary and motivated by altruistic goals.

This thesis will examine whether the law regulates the operation of incorporated associations in a manner that is proportionate, effective and to a standard that is acceptable. In particular, it will compare the raft of statutory duties and obligation of an incorporated association and a for-profit organisation. In examining these specific legal duties, this thesis will reveal the lack of consistency across jurisdictions, and gaps in how the law regulates the conduct of committee members within an incorporated association. Furthermore, this thesis will consider whether an officer of an incorporated and unincorporated association is a fiduciary – and, if this is so, whether this status arises out of the category of principal and agent. Additionally, this thesis will identify specific regulatory and governance issues affecting Australia’s not-for-profit sector.

Finally, this thesis will examine how the numerous federal parliamentary inquiries and government reports intend to develop a reform policy for the not-for-profit sector and to evaluate these policy intentions against the world’s best practice regulatory model.

Keywords: *Incorporated Associations, legal duties, power and control, agency, legal regulatory frameworks, volunteers, social inclusion, federal take-over of the not-for-profit sector.*

Publications arising from thesis research

- The contractual framework governing the relationship between an incorporated association and its members, analysed in this thesis, was discussed in *How Alternative Dispute Resolution has by-passed Incorporated Associations in Queensland*. This paper was presented at the Non-Adversarial Justice Implications for the Legal System and Society Conference of the Australian Institute of Judicial Administration and Monash University (May 2010).
- Aspects of Chapter Five of this thesis, which highlight the need to reform the not-for-profit sector, were presented at the Law and Social Reality, Sydney Law School, Postgraduate Conference. This presentation was entitled *Is a Small Revolution Really Too Much to Ask For?* (October 2010).
- The need to establish statutory legal duties for not-for-profit organisations as an efficient means to address accountability within a not-for-profit was discussed in a paper presented at the 3rd Global Inter-Disciplinary Conference for Crime, Justice and Punishment at Mansfield College, Oxford (September 2011). Inter-Disciplinary Press has published this conference paper entitled *Is there a Perfect Environment for a Villain and Villainess to Survive* in an eBook called *The Real and the Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (ISBN: 978-1-84888-106-8).
- Chapter Nine of this thesis considers whether it is permissible for the federal government, using its power under section 51(xx) of the *Constitution*, to takeover the responsibility of not-for-profit organisations, which would have circumvented the duplication of reporting and registration for not-for-profit organisations. This discussion of section 51(xx) of the *Constitution* was published as an opinion piece in *Viewpoint – Perspectives on Public Policy* entitled *A Federal Takeover of the Not-for-Profit Sector was the Revolution that was Needed – An examination of the Commonwealth's Corporations Power* (Issue 10, October 2012).

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PART I – Introduction

CHAPTER 1: Introduction

1.0 Hypotheses and Objective

The not-for-profit sector and its unique institutions have, in recent times, faced rising public expectations for an improved model of governance. This insistence for not-for-profit entities to be transparent is derived from the perception that they appear and function parallel to a for-profit entity. For example, the Sydney Theatre Company, Australia's largest theatre company, is recorded to be a not-for-profit organisation worth \$30 million dollars.¹ An examination of the Sydney Theatre Company reveals an organisational structure that resembles a large corporation.² Despite the Company possessing the status of a not-for-profit, the organisation undertakes long-term strategic planning and utilises marketing and publicity strategies to raise capital similar to those practices seen in the commercial sector.³

This appearance of not-for-profit organisations operating in a manner akin to a for-profit one has led to numerous misunderstandings surrounding not-for-profit organisations. The core fallacy is that committee members are in a similar position to a company director and, therefore, should be held to account in a manner similar to that of a company director.⁴ Such a proposition serves only as a hindrance to effectively understand the role of a committee member. This thesis will assert the hypothesis that a committee member of an incorporated association is not in the same position as a company director, and a committee member should not be treated as a company director. Furthermore, this thesis will clarify the role of a committee member, which will prove that a committee member and a company director have different roles in their respective organisations. Moreover, not-for-profit organisations continue to present legal problems owing to their *sui juris* nature.

¹ Rosy Mobbs, 'Sydney Theatre Company's Great Revival' (March 2011) *In the Black CPA Australia*, 12–13.

² The organisational form of the Sydney Theatre Company is that of a company limited by guarantee. However, the form of a company limited by guarantee does not always need to be of a hierarchal and formal structure, which is seen within the Sydney Theatre Company. The Sydney Theatre Company has a chairman, a board of directors made up of 13 individuals and a company secretary. There are approximately 300 staff employed by the Sydney Theatre Company and there is no indication whether volunteers are involved with the Sydney Theatre Company. See Sydney Theatre Company Annual Report 2011.

³ See Sydney Theatre Company Annual Report 2011 and, also, Rosy Mobbs, 'Sydney Theatre Company's Great Revival' (March 2011) *In the Black CPA Australia*, 12–13.

⁴ See Keith Fletcher, *The Law Relating to Non-Profits Associations in Australia and New Zealand* (Law Book Company, 1986) 298; Andrew Twaits, 'The Duties of Officers in Non-Profit Organisations (1998) 10(2) *Bond Law Review*, 313.

The not-for-profit sector has made strong contributions both economically and to social wellbeing. In Australia, the economic value of not-for-profit organisations is significant. According to the Productivity Commission, not-for-profit organisations contribute \$43 billion to Australia's Gross Domestic Product (GDP). They claim there are 59,000 economically significant organisations and a 7.7 per cent growth within the not-for-profit sector from 1999/2000 to 2006/2007.⁵ In the same period, volunteer time increased to \$14.6 billion with a 2.2 per cent annual growth in total hours.⁶ This data illustrates the importance of the not-for-profit sector not only in an economic sense, but also to social capital.

The debate for better governance and regulation of this significant economic player is largely based on a corporate rationale that is focused on profit and financial transparency rather than a broader conception of legal duties. The exclusion of legal duties from this debate raises the question, what legal principles guide or should guide an officer of a management committee when discharging their responsibilities. By answering this question this thesis will reinterpret the duties of the management committee, critique the existing law and identify gaps and inconsistencies in the associations statutes and, lastly, review Australia's reform proposals in light of the United Kingdom's best practice model.

Reform within Australia has been confined to two Senate inquiries, a Productivity Commission report, and part of *Australia's Future Tax System, Report to the Treasurer*⁷ (commonly referred to as the 'Henry Tax Review'). As a consequence of these inquiries, sector-specific issues have emerged that require further attention and investigation. This has made the process of reform in the not-for-profit sector slow. In Australia, while there have been reports of charitable organisations failing,⁸ these events have not sparked a reform agenda commensurate to the magnitude undertaken by the United Kingdom. Reform of the not-for-profit sector and its institutions, particularly in the United Kingdom, was in response to the failure (through

⁵ Australian Government Productivity Commission, *Contribution of the Not-for-Profit Sector*, Productivity Commission Research Report (January 2010) XXIV.

⁶ Australian Government Productivity Commission, *Contribution of the Not-for-Profit Sector*, Productivity Commission Research Report (January 2010) 53.

⁷ December 2009.

⁸ Celebrity, Tania Zaetta's charity, Peace for the Children, held a number of fundraising events that raised approximately \$22,000. However, an audit report revealed less than a quarter of the charity's income was distributed to its charitable projects. Josh Robertson, 'TV Celebrity Tania Zaetta's Peace for the Children Charity forced into Suspension, Funds Transferred', *The Courier-Mail*, (online), 9 May 2011 <http://www.news.com.au/entertainment/celebrity/tv-celebrity-tania-zaetta-has-charity-peace-for-the-children-forced-into-suspension/story-e6frfmqi-1226052181710?from=igoogle+gadget+compact+news_rss>.

mismanagement) of notable charities.⁹ The cornerstone of reform in the United Kingdom was in expanding the powers of the Charity Commission to achieve better regulation of the sector.¹⁰ Furthermore, the United Kingdom modernised its not-for-profit sector by introducing new and innovative forms of not-for-profits, and taking proactive measures to increase public and donor confidence in the sector. Legislative provisions were introduced in the United Kingdom to encompass the principles of governance, which not only include financial accountability, but also legal duties.

This thesis will outline the path Australia is currently taking to reform the sector. It will identify the pitfalls of Australia's proposed reform by comparing our model of regulation against world's best regulatory practice from the United Kingdom. To contribute to this area of law, this thesis will also argue that a governance framework for not-for-profit organisations should be underpinned by legal duties appropriate to this area.

1.1 Research Approach and Methodology

The research approach employed for this thesis is multidisciplinary, broad and cross-jurisdictional. This method involved reviewing and analysing key principles of law, in addition to specific theories from the disciplines of economics, social and political sciences. With respect to the cross-jurisdictional aspects, this research includes the examination and analysis of both primary and secondary sources of law from Australia and the United Kingdom.

The design of this research is fundamentally doctrinal. To identify the gaps in the current body of knowledge, research was gathered that included:

- reviewing and analysing economic and social science literature to understand the formation of the not-for-profit sector;

⁹ M. Gibelman and S. Gelman, 'Very Public Scandals: Nongovernment Organization in Trouble' (2001) 12 (1) *Voluntas: International Journal of Voluntary and Nonprofit Organizations* 49, 52–43. In Scotland, an independent regulator was appointed to make changes to charity laws in response to the Breast Cancer Research (Scotland) scandal. Mr Tony Freeman, trustee of Breast Cancer Research (Scotland) and sole director of a fundraising company, Solutions RMC, would sell lottery tickets to the public to raise funds for the charity, which provided treatment and promoted research into the causes of breast cancer. Mr Freeman's trading company had an agreement with the charity that ensured that he received more than half the funds raised from the charity's lottery tickets, box collections and stalls. 'Cancer Charity Accounts Frozen', *BBC News* (online), 23 May 2003 <<http://news.bbc.co.uk/2/hi/uk/scotland/2932624.stm>>.

¹⁰ The United States of America requires all charities, just like corporations, to be subject to the *Sarbanes-Oxley Act of 2002*, Pub L No 107-204, 116 Stat 745. However, in the United Kingdom the Charity Commission regulates all activities of charities and other forms of not-for-profit organisations.

- reviewing and analysing statutory duties for Australian corporations and incorporated associations in all jurisdictions of Australia;
- reviewing and analysing future policy developments for the not-for-profit organisations; and
- reviewing and analysing world's best practice for regulating the not-for-profit sector.

The cumulative effect of this research design will contribute to a better understanding of the role a management committee performs within an incorporated association, to reveal the lack of consistency across jurisdictions, and gaps in how the law regulates the conduct of committee members within an incorporated association.

1.2 Structure

This thesis is arranged into three parts made up of nine chapters as follows:

PART I – Introduction

Chapter One provides an introduction outlining this thesis' objectives and hypothesis, and research methodology. It details the terminology used throughout the thesis and summarise the results and recommendations, with consideration of the limitations encountered throughout this research. It also outlines the contribution this thesis will make to the research of incorporated associations.

Chapter Two defines the structural-operational features of a non-profit organisation through identifying universal characteristics such as, private, organised, voluntary and non-distribution of profit and self-governing. By identifying these broad characteristics, the function and the role of the not-for-profit sector will be examined using an interdisciplinary framework of economic, social-origin and political theories.

PART II – An Inter-Disciplinary Understanding of the Not-for-Profit Sector and Its Organisations

Chapter Three provides a historical perspective of the incorporated association in Australia. Particularly, this chapter focuses on the creation of an incorporated association in South Australia (1858) through to the introduction of this entity in Queensland (1981). The motivating purposes

behind the creation of a new legal entity for not-for-profits was due to the difficulties individual trustees experienced in managing a charitable trust's property. Chapter Three also examines the historical enactment of New Zealand's association legislation. Furthermore, it discusses the advanced features of New Zealand's model of incorporation, which was developed by Sir John Salmond.

Chapter Four outlines the legal structures and their unique features of an association, unincorporated association, incorporated association, and a company limited by guarantee. This analysis will illustrate how the law treats each form differently.

Chapter Five critically analyses and compares the role of a company director and an officer of a management committee. It further analyses and compares statutory duties for a company director and an officer of a management committee, and undertakes an inter-jurisdictional analysis of the legal duties within state association legislation. Furthermore, this chapter explores the persistent question of whether there is a lack of statutory duties and fiduciary principles to provide a committee member with legal obligations. There exist a number of doubtful cases on this point, and this chapter will consider the hesitation by the courts to recognise that a committee member's conduct should be subject to legal obligations. This chapter also argues that the rules governing the relationship of principal and agent are applicable to individual committee members of incorporated and unincorporated associations.

PART III – Shaping Australia's Not-for-Profit Sector for the Future

Chapter Six outlines the numerous inquiries and reports that have been commissioned by the Australian Parliament in recent times. Emerging from all of these inquiries and reports is the call for urgent reform in a diverse range of areas, such as a new definition of charity, and implementing a framework to improve the measurement of the not-for-profit sector. Due to the breadth of reports, Chapter Six will briefly discuss the findings and recommendations relating only to transparency and governance from two key reports: (i) the Australian Government's response to the disclosure inquiry; and (ii) the Productivity Commission's report.

Chapter Seven examines the United Kingdom's not-for-profit sector by outlining the modern forms of not-for-profit organisations and the development of the Charity Commission. Included in this Chapter is a detailed analysis of a trustee's statutory duties and responsibilities, and the

Charity Commission's wide regulatory powers to enforce trustees to meet their legal obligations. Chapter Seven also outlines the powers of the Charity Commission to ensure the proper administration of all not-for-profit organisations in the United Kingdom.

Chapter Eight outlines the proposed reform picture so far in Australia. The prevailing demand emerging from both parliamentary inquiries and the Productivity Commission's report was to embrace the world's best practice regulatory model from the United Kingdom. However, the federal government has rejected this suggestion and has established its own regulating authority. This chapter critiques Australia's proposed statutory regulatory authority.

The centrepiece of this new regulatory system is the establishment of the Australian Charities and Not-for-Profits Commission. Chapter Eight outlines the functions, powers and authority of that the Australian Charities and Not-for-Profits Commission has in relation to the regulation of a specific type and sub-type not-for-profit organisation. This chapter also analyses the ACNC's functions and powers to achieve transparency and restore public trust in the sector.

Chapter Nine compares the functions and the power of the Australian Charities and Not-for-Profits Commission to the United Kingdom's Charities Commission, and reveals numerous limitations of the Australian proposed regulatory framework. These limitations are a consequence of the federal government being concerned with enacting its social inclusion policy rather than reforming the sector to be sustainable into the future. This chapter briefly explains Australia's social inclusion policy and how it will create a fiscal paradigm with government and not-for-organisations. It also discusses the known negative impact social inclusion policy has had on the not-for-profit sector and not-for-profit organisations and assess whether Australia is taking the proactive steps needed to avoid the pitfalls of the social inclusion policy. Furthermore, this chapter discusses how the federal government could have used its power under section 51(xx) of the *Constitution* to takeover the responsibility of not-for-profit organisations, and explains how this would have circumvented the duplication of reporting and registration for not-for-profit organisations.

1.3 Terminology

Not-for-Profit Organisation – An organisation that imposes the principle of the non-distribution of profits to the organisations' members. In this thesis, not-for-profit organisations will encompass all not-for-profit forms, unless otherwise stipulated.

Governance – The monitoring of management's decisions to benefit the company or members and the purpose of a not-for-profit organisation.

1.4 Research Contribution and Outcomes

This thesis aims to broaden the discussion regarding governance within the not-for-profit sector to include legal duties. The current body of knowledge regarding legal duties for the not-for-profit sector is slight, and this thesis will contribute to the literature by:

- providing an analysis of all the statutory duties across Australia's state jurisdictions for an incorporated association, and a comparison with a company director's statutory duties;
- proving there is a legal theoretical basis through agency law that a committee member of an incorporated or unincorporated association is subject to general legal duties;
- providing a theoretical basis for legal duties to be an integral aspect of a governance framework to regulate a committee member's behaviour; and
- critically considering the latest reform proposals.

1.5 Limitations

This thesis is limited to a presumption that committee members will inevitably sometimes behave in contradiction of the association's altruistic mission. Characterising all committee members as potentially opportunistic and dishonest supports the need to introduce legal duties to regulate the conduct of a committee member. However, the real likelihood of either the courts or the legislators imposing legal duties on committee members is limited, unless the association is incorporated as a company limited by guarantee or there is an express provision in the state legislation.

A further limitation to this thesis relates to the ongoing sector development occurring at a federal level. All attempts have been made to include the most recent updates regarding regulation and governance, but this is like shooting at a moving target.

PART II

An Inter-disciplinary Understanding of the Not-for-Profit Sector and its Organisations

CHAPTER 2:

The Definition and Dynamic of the Not-for-Profit Sector

*The role of third sector organisations is giving a voice to many and varied interests.*¹¹

2.0 Introduction

The not-for-profit sector and its institutions have become a valuable and an entrenched feature in contemporary society.¹² At some point in our lives it is inevitable we will have some level of contact with one or more non-profit groups.¹³ An individual's level of contact or involvement with a non-profit organisation can be mixed due to the divergent purposes or mission, activity and size of an organisation. The sizeable organisations within the not-for-profit sector have made it an increasingly challenging task to clearly differentiate between a not-for-profit organisation, a public agency, and a profit organisation. This challenge illuminates the complexity and behaviour of a not-for-profit organisation that have blurred the sectors' boundaries. It has been argued that non-profit organisations are more like for-profits in disguise,¹⁴ which has led to many attempts to produce a steadfast meaning of a not-for-profit organisation.

Chapter Two first defines and classifies the structural-operational features of the non-profit sector by identifying the universal characteristics that are intrinsic, recurrent and operating within it. Identifying these characteristics and the appropriate taxonomy of the non-profit sector is pivotal to understanding how not-for-profit organisations have evolved. This is explored through an interdisciplinary framework of economic, social-origin and political theories.

¹¹ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin, 2001) 20.

¹² The Australian Bureau of Statistics (ABS) reports that in 2006–07 the not-for-profit sector contributed \$43 billion to Australia's Gross Domestic Product (GDP). Further, the ABS has identified a strong growth in the not-for-profit sector by 7.7 per cent from 1999–2000 to 2006–2007. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) Terms of Reference XXVI.

¹³ Kim Weinert, 'How Alternative Dispute Resolution has by-passed Incorporated Associations in Queensland' (Paper presented at Non-Adversarial Justice Implications for the Legal System and Society Conference of the Australian Institute of Judicial Administration and Monash University, Melbourne, 4 May 2010).

¹⁴ Jill Horwitz, 'Does Nonprofit Ownership Matter?' (2007) 24 *Yale Journal on Regulation* 139, 141.

2.1 Characteristics of the Non-Profit Sector

2.1.1 Terminology

Numerous labels or terms have been ascribed to the not-for-profit sector in an attempt to accurately define the sector:¹⁵

- *Charitable sector* – The concept of charity represents the collective moral strength of a sector that contributes to society in a non-exploitive manner.¹⁶ This particular form must benefit the public and have the capacity to carry out its intended purposes.¹⁷ However, this term emphasises and describes only one type of a non-profit organisational form and overlooks all the other different forms in the wider sector.¹⁸
- *Independent sector* – A term suggesting that these organisations are outside the reach of government and private business. In actuality, a significant number of not-for-profit organisations rely on government funding and donations from private business for revenue.¹⁹ Furthermore, it is not uncommon to find an employee of a company that has made a monetary donation to be appointed as an officer of the not-for-profit organisation. These arrangements do not make not-for-profit organisations truly independent.²⁰
- *Tax-exempt sector* – Initially this term appears to be incongruent to this sector. However, it emphasises the fact that organisations generally benefit from many tax advantages. Nevertheless, the term is misleading and is an inadequate description because not all non-profit organisations receive the same favourable tax concessions. For example, in Australia, a charitable organisation will not be taxed on the revenue the organisation earns from fundraising activities. However, a charitable organisation in Russia pays 24 per cent corporate profit tax on most of its revenue. Further, Russian not-for-

¹⁵ Lester Salmon and Helmut Anheier, 'In Search of the Nonprofit Sector I: The Question of Definitions' (Working Paper No 2, The Johns Hopkins Comparative Nonprofit Sector Project, The Johns Hopkins Institute for Policy Studies, June 1992) 4.

¹⁶ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 12.

¹⁷ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 12–13.

¹⁸ Helmut Anheier, *Nonprofit Organisations Theory, Management, Policy* (Routledge, 2005) 38.

¹⁹ Chapter Nine of this thesis outlines the increased reliance that not-for-profit organisations have on government contracts and private funding and the negative impact this reliance has the sector's independence.

²⁰ Helmut Anheier, *Nonprofit Organisations Theory, Management, Policy* (Routledge, 2005) 38. Chapter Nine of this thesis discusses how not-for-profit organisations have come to heavily reliant on government funding.

profits are susceptible to additional taxation if the organisation fails to use monetary gifts within a specified timeframe.²¹

- *Voluntary sector* – This term signifies the input of individuals who volunteer their time and effort into the operation of their organisation with no expectation of compensation. However, the personnel of a not-for-profit organisation today is a mix of paid staff and volunteers.²²
- *Non-governmental (NGO) sector* – Describes a non-government organisation, commonly found in the developing world, that engages and develops economic promotion and social development programmes.²³
- *Économie sociale* – A common term found within the European Union that embraces business-type organisations, such as mutual insurance companies, cooperatives, and saving banks.²⁴ For these organisations to fall within the not-for-profit sector, they must satisfy the following criteria: (i) the organisation's purpose is to serve its members or a larger part of a community; (ii) management is independent from external influences, such as governments; (iii) there is a democratic decision-making process; and (iv) the distribution of income is to serve certain social aspects rather than serving capital investment.²⁵
- *Third sector* – A generic term that describes a sector that coexists with the market and the state.²⁶ Within the third sector, there are organisations that are not part of the public and private sector.²⁷

²¹ Australian Taxation Office, Tax Concessions – An Overview – Tax Basics for Non-Profits Organisations <<http://www.ato.gov.au/nonprofit/content.asp?doc=/content/33743.htm&mnu=45419&mfp=001/004>>. The tax treatment of not-for-profit organisations in Russia illustrates that attempts to define the sector by one feature of a not-for-profit organisation ignores the differentiation in treatment by other countries and their value of non-profit organisations in other societies. Leslie Lutz, 'Economic Constraints, Political Motives: Contemporary Russian Nonprofit Tax Law' (2005) 7(3) *The International Journal of Not-for-Profit Law* 73, 82 <http://www.icnl.org/knowledge/ijnl/vol7iss3/art_4.htm>.

²² Helmut Anheir, *Nonprofit Organisations Theory, Management, Policy* (Routledge, 2005) 38.

²³ Similar to the term 'charity sector', this term too describes only one type of organisation within the not-for-profit sector. Helmut Anheir, *Nonprofit Organisations Theory, Management, Policy* (Routledge, 2005) 39.

²⁴ Helmut Anheir, *Nonprofit Organisations Theory, Management, Policy* (Routledge, 2005) 39.

²⁵ Helmut Anheir, *Nonprofit Organisations Theory, Management, Policy* (Routledge, 2005) 39.

²⁶ Sybille Mertens, 'Nonprofit Organisations and Social Economy: Two Ways of Understanding the Third Sector' (1999) 70(3) *Annals of Public and Cooperative Economics* 501.

²⁷ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin, 2001) 5-9.

Each of these wide and varied terms have proved to be inadequate as they confine the description of the sector to only one emphasised organisational feature – they overlook the many other distinctive features of a not-for-profit organisation.²⁸ This thesis does not seek to redefine nor rename the sector. Therefore, the generic term ‘not-for-profit’ will be used throughout this thesis.

Just like there are many labels used to explain not-for-profits, there have been many attempts to find a universal and accepted taxonomy (definition and classification) of this sector.

2.2 Defining the Not-for-Profit Sector

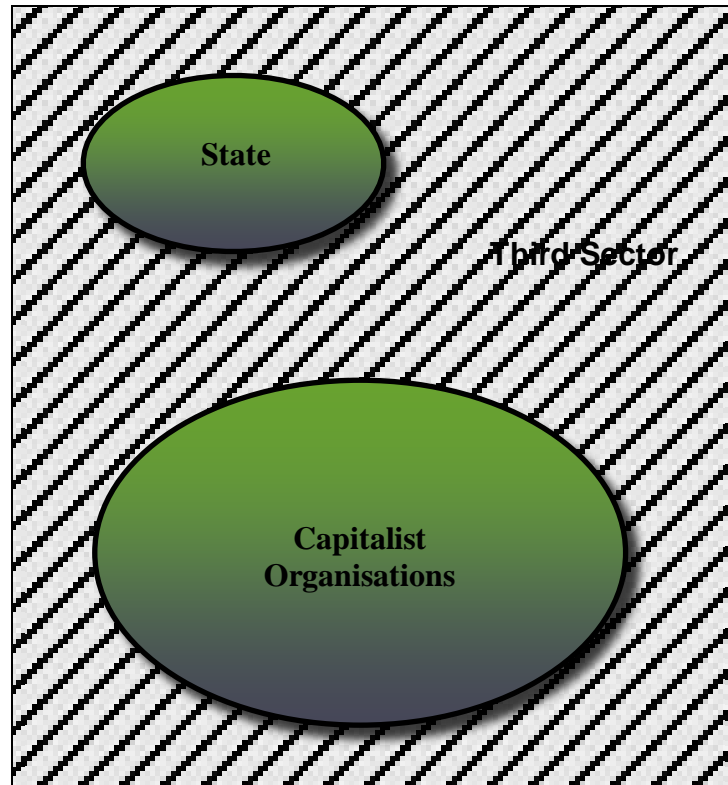
It is important to understand the space in which the not-for-profit sector resides. It was in the late 1970s that Jacques Delors described this sector as a ‘phenomenon’.²⁹ Delors found small production units that were initiated by community groups or individuals and employed collective work practices to meet a genuine need.³⁰ These production units were neither the church nor a capitalist enterprise controlled by the state. Named by Delors as a ‘third sector’, these production units were initially considered to be a residual group that fell outside the two other well-defined sectors, as illustrated in Figure 1.

²⁸ Lester Salamon and Helmut Anheier, ‘In Search of the Nonprofit Sector I: The Question of Definitions’ (Working Paper No. 2, The Johns Hopkins Comparative Nonprofit Sector Project, The Johns Hopkins Institute for Policy Studies, June 1992) 2.

²⁹ Sybille Mertens, ‘Nonprofit Organisations and Social Economy: Two Ways of Understanding the Third Sector’ (1999) 70(3) *Annals of Public and Cooperative Economics* 501, 501-502.

³⁰ Sybille Mertens, ‘Nonprofit Organisations and Social Economy: Two Ways of Understanding the Third Sector’ (1999) 70(3) *Annals of Public and Cooperative Economics* 501, 502.

Figure 1 – The space where the third or the not-for-profit sector exists³¹



The acceptance of the third space existing outside of the market (private) and state (public) lead to the discovery that this new space hosted a dynamic and diverse range of organisational entities.³² These entities, or institutions, were also found to be very different to those in other conventional sectors.³³ The unique nature of these entities reveals a combination of private structure with a public purpose connecting with citizens, by being:

- flexible and informal;
- capable of supporting public purposes; and
- proficient in performing vital functions in partnership with the state and the market, such as delivering essential human services in health care.³⁴

³¹ Sybille Mertens, 'Nonprofit Organisations and Social Economy: Two Ways of Understanding the Third Sector' (1999) 70(3) *Annals of Public and Cooperative Economics* 501, 502.

³² For example, hospitals, universities, sport clubs, environmental groups, professional organisations, religious congregations, job training centres, shelters for women and the homeless, soup kitchens, schools and many other entities. Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 168; Lester Salamon and Helmut Anheier, 'In Search of The Nonprofit Sector I: The Question of Definitions' (Working Paper No. 2, The Johns Hopkins Comparative Nonprofit Sector Project, The Johns Hopkins Institute for Policy Studies, 1992) 1.

³³ Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 168 -169.

³⁴ Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 168 -169.

Furthermore, these entities within this third space empower the disadvantaged by bringing unaddressed problems to the public's attention, building community bonds of trust, and allowing individuals to mobilise an initiative in pursuit of a common good.³⁵ The function of these production units is outside of the traditional 'two-model' approach and should be analysed further.

Taking an analytical look at the not-for-profit sector and its entities will provide an insightful understanding about the function of the not-for-profit sector and its institutions. The understanding gained from this analysis will subsequently support a clear definition of a not-for-profit organisation. Knowing what constitutes a not-for-profit organisation means that the task of differentiating a not-for-profit from other units (such as government agencies and private business) can be done with precision.³⁶ Additionally, the formation of a clear definition of a not-for-profit organisation was imperative to Lester Salamon's comparative study. The primary aim of this study was to identify and measure the contribution of not-for-profits domestically and cross-nationally.³⁷

Prior to the formation of the universal definition, the comparative analysis needed to be capable of identifying a not-for-profit organisation. The study initially found and outlined certain common features that numerous not-for-profit institutions possessed.³⁸ Table 1 provides a summary of these commonalities.

³⁵ Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 168 -169.

³⁶ Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 172-174.

³⁷ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 4.

³⁸ Lester Salamon and Helmut Anheier, 'In Search of The Nonprofit Sector I: The Question of Definitions' (Working Paper No. 2, The Johns Hopkins Comparative Nonprofit Sector Project, The Johns Hopkins Institute for Policy Studies, June 1992) 12-13.

Table 1 – Distinctive features of not-for-profit institutions³⁹

Feature	Description
Production Function	Unlike for-profit companies and the state, not-for-profits do not exist or function to generate and/or distribute profits, or use force like the state. While it is acceptable for a not-for-profit to make a profit, the organisation is not to be the personal source of financial gain for its members or directors.
Public Goods	The production of goods and services by not-for-profits is aimed at delivering benefits to the broader community and, also, to its members. It is more difficult for a not-for-profit to finance the production of such goods and services. ⁴⁰
Governing Structures	Members or a self-perpetuating board of private citizens have the control of an entity. Unlike the state the entity are not governed by public elections.
Revenue Structure	Not-for-profits receive revenue from a number of sources including donations, membership fees and government contracts.
Staffing Structure	Not-for-profits rely on a combination of volunteer and paid labour.
Tax Treatment	Not-for-profits receive tax advantages, which include an exemption from many taxes and eligibility for tax-deductible gifts.
Legal Treatment	The law treats and regulates not-for-profits differently to for-profit companies.

Salamon considered these distinctive features were not enough to support a clear universal definition of a not-for-profit organisation.⁴¹ After closely scrutinising a range of definitions, Salamon believed that it was important to establish a definition that encompassed all the salient features that could be applied cross-nationally.⁴² Emerging from this stage of Salamon's analysis are five structural-operational features that are the hallmark of a not-for-profit entity.⁴³ Termed the 'structural-operation definition', Table 2 explains these five key characteristics.

³⁹ Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 172–174.

⁴⁰ Part 2.4 of this thesis explains cost inefficiencies which not-for-profit organisations face when producing public goods.

⁴¹ Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 174.

⁴² Salamon considered the legal, economic, normative and functional definitions, but found each of them problematic for his cross-national comparative study. Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 174–175.

⁴³ Organisations that do not satisfy all of these five characteristics of the structural-operational definition are not not-for-profit entities. Helmut Anheier, *Nonprofit Organisations - Theory, Management, Policy* (Routledge, 2005) 47.

Table 2 – The five characteristics of the structural-operation definition⁴⁴

Feature	Description
<i>Organised</i>	To be termed ‘organised’ an entity must display a degree of organisational structure or boundaries. For an organisation to have any real or meaningful identity there must be regularity to the organisation’s operation demonstrated by regular meetings, rules of procedures or some other degree of organisational performance. Excluded from this specific characteristic are ad hoc and temporary gatherings of people such as, friendship circles and families. ⁴⁵
<i>Private</i>	The entity is separate from, or is no part of the government apparatus at a national or local level and does not exercise any government authority. ⁴⁶ It is important that an organisation has and maintains a separate institutional identity to any unit of the state. ⁴⁷
<i>Self-governing</i>	The entity is capable, through its own mechanisms of control and autonomy to be self-governing. This is illustrated by the entity’s management to have the ability to change their by-laws and their internal structure, alter their missions or goals and capable of dissolving the entity without the permission of another authority. ⁴⁸
<i>Non-Distribution of Profit</i>	Where an entity has accumulated a surplus or a profit, in any given year, it is strictly forbidden to distribute this profit to its members, owners, founders or governing board. Any profit attained by the entity must be redistributed or re-invested in the entity’s mission or objectives. ⁴⁹
<i>Non-Compulsory or Voluntary</i>	An individual’s participation must be voluntary, not enforced, nor a requirement by law, or a condition of citizenship. Where it is imperative to an individual’s employment to be a member of a professional organisation, this type of organisation is not considered a not-for-profit organisation and therefore is excluded from the not-for-profit sector. ⁵⁰

Once the structural-operation definition was in place, the next stage of the comparative study involved developing a classification scheme that used the commonalities of not-for-profit organisations.

⁴⁴ United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 18.

⁴⁵ Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 47; United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 18.

⁴⁶ There are not-for-profit organisations that do exercise government authority, which is delegated, determined and administered to the organisation by the state; moreover, the not-for-profit organisation does not have sovereign authority. United Nations Handbook of Accounts, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 19.

⁴⁷ Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 47; United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 19.

⁴⁸ United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 19-20.

⁴⁹ United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 18-19. The characteristic of non-distribution of profit is examined further in this thesis.

⁵⁰ United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 20.

2.3 International Classification of Not-for-Profit Organisations

The aim of the classification scheme is to outline where not-for-profit organisations differ in purpose and activity from the other two sectors.⁵¹ These components make it simpler to create sub-groups that highlight the particular focus of each not-for-profit organisation in the context of its country.⁵² The usefulness of this classification scheme is central to an economic analysis, reporting and policy development. Table 3 is a summary of the international classification scheme, which is used at an international level, but there are other several classifications in existence.⁵³

Table 3 – International classification of not-for-profit organisations⁵⁴

Group	Description and Activity
Group 1	<i>Culture and Recreation</i> <ul style="list-style-type: none">• Culture and arts• Sports• Other recreation (service organisations)
Group 2	<i>Education and Research</i> <ul style="list-style-type: none">• Primary and secondary education• Higher education (university)• Other education (vocational, technical or adult)• Research
Group 3	<i>Health</i> <ul style="list-style-type: none">• Hospitals and rehabilitation• Nursing homes• Mental health and crisis intervention• Other health services (public health and wellness education, outpatient services or emergency services)
Group 4	<i>Social Services</i> <ul style="list-style-type: none">• Social services• Emergency and relief• Income support and maintenance

⁵¹ Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 54.

⁵² United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions into the System of National Accounts* (2003) 32.

⁵³ The United States of America's national taxonomy of tax-exempt entities is used to classify not-for-profit organisations based on an organisation's major activities. Helmut Anheier, *Nonprofit Organisations - Theory, Management, Policy* (Routledge, 2005) 54.

⁵⁴ United Nations Handbook of National Accounting, *Handbook on Non-Profit Institutions in the System of National Accounts* (2003) 31.

Group 5	<i>Environment</i> <ul style="list-style-type: none"> • Environment • Animal protection
Group 6	<i>Development and Housing</i> <ul style="list-style-type: none"> • Economic, social and community development • Housing • Employment and training
Group 7	<i>Law, Advocacy and Politics</i> <ul style="list-style-type: none"> • Civic and advocacy organisations • Law and legal services • Political organisations
Group 8	<i>Philanthropic Intermediaries and Voluntarism Promotion</i> <ul style="list-style-type: none"> • Grant-making foundations • Fundraising organisations
Group 9	<i>International</i> <ul style="list-style-type: none"> • Development assistance services • International disaster and relief organisations • International human rights and peace organisations
Group 10	<i>Religion</i> <ul style="list-style-type: none"> • Promoting of religious beliefs • Administering religious services and rituals
Group 11	<i>Business and Professional Associations and Unions</i> <ul style="list-style-type: none"> • Professional and organisations • Business associations • Trade unions
Group 12	<i>Not Elsewhere Classified</i>

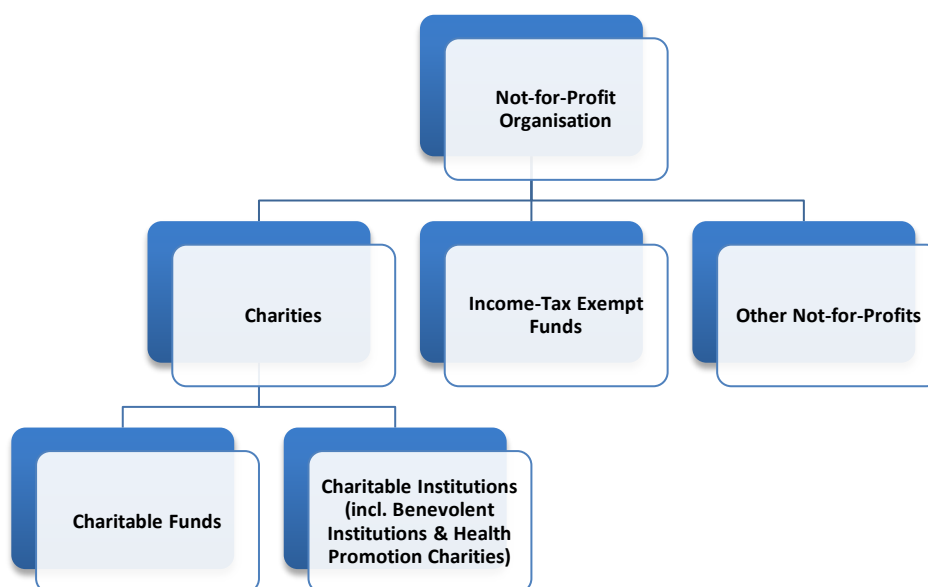
This immense collaborative effort sensibly framed a miscellany of features, size, organisations and activities for the not-for-profit sector. The international classification scheme has been adopted by the Australian Bureau of Statistics (ABS) to develop a measuring framework to capture data on the not-for-profit sector and its organisations.⁵⁵ Australia's recent adoption of the international classification scheme is an improvement on the previous classification scheme used by the Australian Taxation Office (ATO).

The classification model used by the ATO is best described as one-dimensional. The ATO's model is confined to identifying the structure of the organisation (whether the entity is a charity

⁵⁵ Senate Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) Chapter 2
http://www.aph.gov.au/senate/committee/economics_ctte/charities_08/report/c02.htm.

or not), albeit for taxation purposes (see Figure 2). Unlike the international classification scheme, the ATO does not capture information on the organisation's missions or activities and, furthermore, it overlooks whether it is within the existing taxation system or not.⁵⁶ Another criticism that can be levelled at the ATO's classification system is that it does not allow for an in-depth exploration of these organisations or the internal and external influences that may affect them.⁵⁷ Chapter Eight of this thesis outlines the new statutory authority's shared responsibility with the ATO regarding the classification of not-for-profit organisations.

Figure 2 – Australia's classification model for not-for-profit organisations⁵⁸



Salamon's international comparative study broke through some misconceptions of not-for-profits by providing a clear definition of them, and used for data gathering. Reports generated from this data offer a credible statistical snapshot of the sector's economic contribution. However, data alone cannot provide an absolute explanation as to why the sector and its organisations function in the manner that is different to the other two sectors. Economic and socio-political theories

⁵⁶ Organisations are registered for taxation purposes if they: employ staff; accept tax-deductible donations; pay income tax; seek exemption from fringe benefit tax or concessional input tax treatment; or are subject to Goods and Services Tax (GST). All not-for-profit organisations with an annual turnover of \$150,000 or more must be registered for GST, and organisations below this turnover threshold may choose to be registered for GST. The downside to the ATO's classification scheme is that small not-for-profit organisations with little revenue or no staff are not considered to exist for the purpose of ATO's recordings. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 59.

⁵⁷ Denise Crossan and Jon Van Til, 'The Third Sector and Sustainable Social Change: New Frontiers for Research' (Paper Presented at 2nd EMES-ISTR European Conference, Barcelona, Spain 9-12 July 2008) 5.

⁵⁸ Australian Taxation Office, 'Guide for Non-Profit Organisations – Tax Basics for Non-Profit Organisations' (June 2011) 5.

focus on understanding the origin of the not-for-profit sector and explain the behaviour of not-for-profit organisations.

2.4 An Economic Understanding of the Not-for-Profit Sector

As illustrated in Chapter One, the economic contribution of this sector in Australia is sizable.⁵⁹ The not-for-profit sector is a commanding economic player, and economists have strived to develop a number of theories hypothesising why not-for-profits exist. As Jacquelyn Thayer-Scott remarks, economists define the not-for-profit sector and its activities only within the theoretical framework of conventional market economies, and this is prevalent in Professor Burton Weisbrod's research.⁶⁰ In 1975, Weisbrod applied conventional economic theories of market failure and public goods to the not-for-profit sector to find out what causes not-for-profit organisations to exist.⁶¹ To find the answer question, he astutely drilled down to ask:

- a. what determines that certain goods are to be provided by the government, the for-profit, and not-for-profit markets?
- b. are there predictable circumstances in which the not-for-profit sector will develop, grow and decline?⁶²

Basic economic theory states that markets will, under particular conditions, fail and when market failure occur; governments only exist to address some of these failures.⁶³ The main example of

⁵⁹ In 2006–2007 it was reported that the not-for-profit sector accounted for 4.1% of Australia's GDP, and employed approximately 890,000 people with a further 4.6 million volunteering their services. Further, about three-quarters of volunteers across all not-for-profit organisations contribute to activities that are cultural and recreational in nature or to social services. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 53.

⁶⁰ Jacquelyn Thayer Scott, 'Defining the Nonprofit Sector' in Paul B. Reed and Valerie J. Howe 'Defining and Classifying the Nonprofit Sector' (Research Paper, Statistics Canada and Carleton University, 1999) 47 <<http://dsp-psd.pwgsc.ca/Collection/statcom/75F0048m1/2002207.pdf>>

⁶¹ Market failure is where there is a voluntary exchange of goods and services that fails to reach an efficient outcome. Where there is a production, goods under these conditions will create a spill over cost. This negatively affects a third party associated with the exchange. Consequently, the third party will bear the costs and will not be compensated by any corresponding benefit. When there is a negative externality, the market will overproduce goods. This occurs when the trading parties fail to account for all additional costs, called the social marginal costs of production. On the flip side, there is positive externality, which has a spill over benefit. Here, a third party enjoys a benefit of the other trader's actions without paying. The third party is called a free rider. When there is a positive externality, the market under-produces goods. If the free rider is willing to pay for the goods, it will result in more production. Where there is no incentive for free riders to pay, then the opportunity of a mutually beneficial exchange remains exploited. Peter Boettke and David Prychitko, 'Is an Independent Nonprofit Sector Prone to Failure? An Austrian School Analysis of the Salamon Paradigm and the Lohmann Challenge' (Working Paper No 15, Mercatus Centre, George Mason University, undated) 10-11 <<http://ssrn.com/abstract=1538370>>.

⁶² Al Slivinski, 'The Public Goods Theory Revisited - Comments on Kingma's Revisitation of Weisbrod' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises – Theories and Approaches* (Academic/Plenum Publishers, 2005) 68.

market failure is the production of a public good.⁶⁴ Economists characterise goods by their availability and allocation,⁶⁵ as well as the properties of ‘non-rivalrousness’ and ‘non-excludability’.⁶⁶ Non-rivalrousness means that once a unit of a good or service is produced, it may be consumed and enjoyed by an individual without detracting the consumption opportunities available to others.⁶⁷ The second characteristic, non-excludability, denotes that it is impossible to exclude a user from enjoying a good or service if the user does not pay for the good or service.⁶⁸ A clear example of a public good is national defence.⁶⁹ National defence is both non-excludable and non-rival – private firms, under pure market conditions, will not produce these goods, as they cannot cover their costs or make a profit.⁷⁰ This allows the government to utilise their coercive power to provide these goods through taxation and legislation while also aiming to satisfy the median voter.⁷¹ Determining the level of quality and quantities of public goods is a political decision motivated to satisfy the medium voter.⁷²

⁶³ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001) 199.

⁶⁴ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001) 199.

⁶⁵ Bernard Gazier and Jean-Philippe Touffut ‘Introduction’ in Jean-Philippe Touffut (ed) *Advancing Public Goods* (Edward Elgar Publishing, 2006) 1.

⁶⁶ Sometimes referred to as ‘non-rival consumption’. Peter Boettke and David Prychitko, ‘Is an Independent Nonprofit Sector Prone to Failure? An Austrian School Analysis of the Salamon Paradigm and the Lohmann Challenge’ Global Prosperity Initiative Working Paper 15, Mercatus Centre, George Mason University <<http://ssrn.com/abstract=1538370>>, 11

⁶⁷ For example, the presence of a number of people attending a dramatic play will not diminish an individual’s enjoyment of the play. Peter Boettke and David Prychitko, ‘Is an Independent Nonprofit Sector Prone to Failure? An Austrian School Analysis of the Salamon Paradigm and the Lohmann Challenge’ (Global Prosperity Initiative Working Paper 15, Mercatus Centre, George Mason University, undated) <<http://ssrn.com/abstract=1538370>>, 11; Helmut Anhhier, *Nonprofit Organisations - Theory, Management, Policy* Routledge (2005), 117.

⁶⁸ Bernard Gazier and Jean-Philippe Touffut, ‘Introduction’ in Jean-Philippe (ed), *Advancing Public Goods* (Edward Elgar Publishing, 2006) 1.

⁶⁹ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin, 2001) 99.

⁷⁰ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin, 2001) 99.

⁷¹ Richard Cornes and Todd Sandler, *The Theory of Externalities, Public Goods and Club Goods* (Cambridge University Press, 2nd ed, 1999), 9. It is difficult, if not impossible, to keep free riders from enjoying the public good except at great costs. For instance, it would be costly, if not impossible, to exclude non-taxpayers from benefiting from a public good like national defence. Peter Boettke and David Prychitko, ‘Is an Independent Nonprofit Sector Prone to Failure? An Austrian School Analysis of the Salamon Paradigm and the Lohmann Challenge’ (Working Paper No 15, Mercatus Centre, George Mason University, undated) 11 <<http://ssrn.com/abstract=1538370>>; Helmut Anhhier, *Nonprofit Organisations - Theory, Management, Policy* (Routledge, 2005) 117.

⁷² Al Slivinski, ‘The Public Goods Theory Revisited – Comments on Kingma’s Revisitation of Weisbrod’ in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises - Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 68.

Professor Weisbrod adds to the public goods theory by acknowledging that there will be individuals who will consume more of those public goods financed by the government, and there will be some who will consume other goods that are imperfect substitutes.⁷³ Thus, individuals will turn to the private sector to satisfy their demands. In such circumstances, when will profit-taking firms arise to satisfy this demand? And could a not-for-profit organisation be capable of satisfying that demand?

Professor Weisbrod found that not-for-profit organisations provide public goods from the collective action of the individuals. The types of goods provided by both for profit and not-for-profit organisations are quasi-public goods, not pure public goods. However, it is only not-for-profit organisations that provide quasi-public goods for collective consumption.⁷⁴

Furthermore, Professor Weisbrod found that government provides goods mostly of one variety, which then causes a residual demand for an alternative to public goods. Professor Weisbrod reasoned that in satisfying this residual demand, for-profit organisations provide only privately financed public goods, such as electricity.⁷⁵ Regarding not-for-profit organisations, Weisbrod states that the provision of public goods is a reaction to the failures of both the market and of government to provide alternative goods.⁷⁶ Consequently, not-for-profit organisations provide an imperfect substitute of the public good. The level of reaction, according to Professor Weisbrod, is how not-for-profits emerge, grow, contract and develop as a substitute for state intervention.⁷⁷

When individuals rely on quasi-public goods from not-for-profits, this results in demand heterogeneity. This refers to the demand for public and quasi-public goods across different

⁷³ Al Slivinski, 'The Public Goods Theory Revisited – Comments on Kingma's Revisitation of Weisbrod' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises – Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 68.

⁷⁴ Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 121.

⁷⁵ Al Slivinski, 'The Public Goods Theory Revisited – Comments on Kingma's Revisitation of Weisbrod' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises – Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 68.

⁷⁶ Al Slivinski, 'The Public Goods Theory Revisited – Comments on Kingma's Revisitation of Weisbrod' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises – Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 68.

⁷⁷ Peter Boettke and David Prychitko, 'Is an Independent Nonprofit Sector Prone to Failure? An Austrian School Analysis of the Salamon Paradigm and the Lohmann Challenge' (Working Paper No 15, Mercatus Centre, George Mason University, undated) 7.

population groups.⁷⁸ The demand from each group will vary in the good's quality and quantity.⁷⁹ For instance, education can be delivered through more than one model. Weisbrod also hypothesised that where there is greater diversity in a society, there will also be a larger set of not-for-profit organisations delivering a diverse set of public goods.⁸⁰ The delivery of the public good can be hampered by the theory of crowding out.

Crowding-out occurs when government either supports the public good itself, or fund not-for-profits for the provision of those public goods.⁸¹ While crowding out will equate to a dollar-to-dollar basis, it rests on a trade-off relationship between the state and not-for-profit sector.⁸² This is illustrated when there is an increase in governmental services responding to the demand of a non-median voter. This will impact on the level of the not-for-profit's activities and, subsequently, not-for-profit organisations will seek diversity in other revenue-generating activities and areas.⁸³ The expansion of not-for-profits, according to Lester Salamon, is not due to a government's failure to provide certain goods or services, but rather the action of individuals.

Salamon's independency theory argues that regardless of government and market failure, the not-for-profits existence is as the result the voluntary action of people's social obligation.⁸⁴ Further, Salamon is critical of Weisbrod's theory by asserting that not-for-profit organisations and governments are not insulated from each other, but frequently act in a partnership.⁸⁵ This partnership is bound by governmental financial support that underwrites the operation of not-for-profit organisations.⁸⁶ The interdependency theory denotes that a number of challenges must be

⁷⁸ Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 121.

⁷⁹ Al Slivinski, 'The Public Goods Theory Revisited – Comments on Kingma's Revisitation of Weisbrod' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises – Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 68.

⁸⁰ Diversity of population means ethnicity, language, religion, age, lifestyle, income, and occupational and professional backgrounds. Helmut Anheier, *Nonprofit Orgnaistions – Theory, Management, Policy* (Routledge, 2005) 121.

⁸¹ Burton Abrams and Mark Schmitz, 'The Crowding-Out Effect of Governmental Transfers on Private Charitable Contributions' in Susan Rose-Ackerman (ed), *The Economics of Nonprofit Institutions: Studies of Structure and Policy* (Oxford University Press, 1986) 303-312.

⁸² Richard Steinberg, 'Overall Evaluation of Economic Theories' (1997) 8(2) *Voluntas* 179, 186.

⁸³ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001) 199.

⁸⁴ Helmut Anheier, *Nonprofit Orgnaistions – Theory, Management, Policy* (Routledge, 2005) 130

⁸⁵ Chapter Nine of this thesis examines the increasing reliance by governments on the not-for-profit sector to deliver public goods and services.

⁸⁶ Salamon has labelled this partnership as 'third party government'. Helmut Anheier, *Nonprofit Orgnaistions – Theory, Management, Policy* (Routledge, 2005) 129–130.

present for the government to be willing to step in and assist with the production of public goods. Such limitations are:⁸⁷

- *Inadequate Resources* – Resources are inadequate due to the free rider problem.⁸⁸ Quasi-public goods being subject to the free rider problem exposes those individuals that benefit from voluntary action and have little or no incentive to contribute. Therefore, the goodwill of a few individuals falls short of what is sufficiently needed to address the welfare and societal problems.
- *Philanthropic Particularism* – Occurs when a not-for-profit organisation focuses only on a sub-group within the organisation, resulting in the duplication of volunteers' efforts as each sub-group demands their own agency or service.
- *Philanthropic Paternalism* – When a not-for-profit organisation lacks accountability and decisions are made on behalf of donors. This creates situations leading to the not-for-profit organisation pursuing activities that benefit only the donors' interests, values, activities and needs, rather than the needs of the organisation.
- *Amateurism* – Volunteers within the not-for-profit organisation may lack the professional skills to deal with wider social problems.

In conclusion, Salamon's independency theory maintains that not-for-profit organisations and governments rely on each other to deliver public and quasi-public goods, which is in contrast to Weisbrod's public goods theory.⁸⁹

Professor Hansmann takes a different approach to explaining the activities of a not-for-profit organisation within our economy. He examines the function of not-for-profit organisations through the conventional economic theory of contract failure. This refers to a failure that exists in the implicit contract between a buyer and a seller, or between a principal and their agent.⁹⁰ Professor Hansamann argues that this failure arises for not-for-profit organisations when there is

⁸⁷ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001) 200; Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 130–131.

⁸⁸ Please refer to footnote 69 for an explanation of the free-rider problem.

⁸⁹ Chapters Nine of this thesis discuss the consequences for not-for-profit organisations that come to rely on government service delivery contracts.

⁹⁰ Henry Hansmann, 'The Role of Nonprofit Enterprise' (1980) 89(5) *The Yale Law Journal* 835, 849.

an imbalance in information between the not-for-profit organisation and the donor, or principal and agent; this is defined as information asymmetry.⁹¹

Information asymmetry, under market conditions, demonstrates that there is a strong incentive to conceal this knowledge and to use it to one's advantage.⁹² Hansmann argues that not-for-profit organisations exist as a response to information asymmetry rather than a response to government failure. This argument is supported by the existence of mutual insurance and other forms of cooperative ownership.⁹³ Information asymmetry commonly occurs in the provision of a complex service, such as health care and welfare. For instance, where a principal, or a not-for-profit organisation, is unable to check the performance of their agent or donor, the contractual relationship allows for an agent to easily exploit the consumer's trust (principal) by providing poor-quality service – or the agents could keep the donation for themselves.⁹⁴ Hansmann strongly believes that not-for-profit organisations are less likely to exploit the information asymmetry than a for-profit firm, therefore making not-for-profit organisations trustworthy.⁹⁵ Another key observation made by Hansmann to explain the basic differences in how a not-for-profit functions relative to its for-profit counterpart is the non-distribution constraint theory.

Already recognised as one of the five features of the structural-operational definition, the 'non-distribution constraint' is the fundamental difference between a for-profit and not-for-profit firm.⁹⁶ Hansmann explained that, regardless of the enormous diversity found in the not-for-profit sector and the various forms of not-for-profit organisations, they are all constrained from distributing its net earnings to any individual who exercises control – such as members, officers, directors or trustees.⁹⁷ Hansmann's trustworthy theory, combined with his non-distribution

⁹¹ Helmut Anheier, *Nonprofit Organisations - Theory, Management, Policy* (Routledge, 2005) 115.

⁹² Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge (2005) 115.

⁹³ Henry Hansmann, 'The Role of Nonprofit Enterprise' (1980) 89(5) *The Yale Law Journal* 835, 846-847.

⁹⁴ Evelyn Brody, 'Agents without Principals: The Economic Convergence of the Nonprofit and For-Profit Organizational Forms' (1995-1996) 40 *New York Law School Law Review* 457, 462; Mark Lyons, *Third Sector - The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001) 200.

⁹⁵ Henry Hansmann, 'The Role of Nonprofit Enterprise' (1980) 89(5) *The Yale Law Journal* 835.

⁹⁶ Henry Hansmann, 'The Role of Nonprofit Enterprise' (1980) 89(5) *The Yale Law Journal* 835, 835-839.

⁹⁷ The presence of the non-distribution constraint principle within Australia's not-for-profit sector is strengthened by law through some of the states' incorporated associations legislation. See *Associations Incorporation Act 1984* (NSW) s 7(1); *Associations Incorporation Act 1981* (Vic) s 10(1)(b); *Associations Incorporation Reform Act 2012* (Vic) ss 4, 33; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 6; *Associations Incorporation Act 1991* (ACT) s 14(1)(b). In Queensland, the non-profit constraint is provided for in the meaning of 'association', *Associations Incorporation Act 1981* (QLD) s 2 Sch. The respective *Association*

constraint principle, clearly illustrates that non-pecuniary preferences serves as the dominant and motivating behaviour of not-for-profit-organisations.⁹⁸ These deep, motivating factors will always trump any opportunistic behaviour or adulteration that is found in for-profit firms.⁹⁹ Hansmann's theories are largely descriptive, which successfully emphasises the predominate features of a not-for-profit organisation; however, an explanation as to how these features operate in the context of the sector is overlooked.

Ortmann and Schlesinger tested the operation of Hansmann's theories against the contemporary realities faced by not-for-profit organisations, which is an increasing demand for their services and goods. This examination revealed Hansmann's theories has the following limitations:¹⁰⁰

- Incentive Compatibility Challenge - The non-distribution constraint principle has been found to hinder a not-for-profit organisation's ability to pursue and develop their own incentives;¹⁰¹
- Adulteration Challenge – The behaviour of individuals that are involved in a not-for-profit should not be adulterated, but there is a realisation that individuals could take advantage of this perceived trustworthiness;¹⁰² and
- Reputational Ubiquity Challenge – Generally, consumers regard a not-for-profit organisation to be reliable, whereas consumers view for-profit organisations as unreliable.¹⁰³

Incorporation legislation of Western Australia, Tasmania and South Australia does not contain the phrase 'any lawful purpose'; however, in these jurisdictions they employ a clearer phrase, 'not for the purpose of financial or pecuniary gain'. This could easily be interpreted in line with the non-distribution constraint principle – see *Associations Incorporation Act 1987 (WA)* s 4(2); *Associations Incorporation Act 1964 (Tas)* s 2 meaning of 'association'; and *Associations Incorporation Act 1985 (SA)* s 18(6). The *Associations Act* in the Northern Territory does not contain a non-distribution constraint provision because this legislation permits trading associations, which results in members of the association receiving a financial gain from the association's profits.

⁹⁸ Vladislav Valentinov, 'Managerial Non pecuniary Preferences in the Market Failure Theories of Nonprofit Organisation' (2009) 39(2) *International Journal of Social Economics* 81, 83.

⁹⁹ Helmut Anheier, *Nonprofit Orgnaistions - Theory, Management, Policy* (Routledge, 2005) 125. Unlike not-for-profits for-profits' behaviour is considered adulterous in order to maximise profits.

¹⁰⁰ Andreas Ortmann and Mark Schlesinger, 'Trust, Repute and the Role of Nonprofit Enterprise' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises - Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 82.

¹⁰¹ Andreas Ortmann and Mark Schlesinger, 'Trust, Repute and the Role of Nonprofit Enterprise' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises - Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 82 -84.

¹⁰² Andreas Ortmann and Mark Schlesinger, 'Trust, Repute and the Role of Nonprofit Enterprise' in Helmut Anheier and Avner Ben-Ner (eds), *The Study of the Nonprofit Enterprises - Theories and Approaches* (Kluwer Academic/Plenum Publishers, 2005) 84.

The two seminal economic theories of Hansmann and Weisbrod explain the existence of the not-for-profit sector; however, these theories overlook the supply-side of economic theory.¹⁰⁴ Entrepreneurship theories justify the existence of not-for-profits from a supply perspective.¹⁰⁵ Ben-Ner and Van Hoomissen state that not-for-profit organisations can be enterprises created by social entrepreneurs,¹⁰⁶ religious leaders, and others who are not motivated by profits.¹⁰⁷

Pursuant to entrepreneurship theory, a not-for-profit organisation will produce goods or services as a means to achieve the organisation's objective. Rather than relying on the collective action of the organisation, it is the social entrepreneur who will drive the primary objective, the outputs, and develop the not-for-profit organisation.¹⁰⁸ True success for a social entrepreneur is to achieve the principal objectives, which equates to the organisation achieving maximising non-monetary returns and utility maximisation.¹⁰⁹

Another example of entrepreneurship theory is commonly found in organised religious groups, which have individuals who are highly motivated to drive a mission. Many religious groups are strategically placed in certain areas to provide an array of goods and/or services. For instance, religious groups provide education by establishing schools, health care by establishing hospitals, and provide other critical support services, such as crisis centres.¹¹⁰ The variety of services provided by an organisation highlights that social entrepreneurs actively find opportunities to maximise the quantifiable aspects by combining service delivery with their

¹⁰³ Andreas Ortmann and Mark Schlesinger, 'Trust, Repute and the Role of Nonprofit Enterprise' in Helmut Anheier and Avner Ben-Ner, Kluwer (eds) *The Study of the Nonprofit Enterprises - Theories and Approaches* (Academic/Plenum Publishers, 2005) 84-85.

¹⁰⁴ Mark Lyons, *Third Sector - The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001) 201.

¹⁰⁵ Susan Rose-Ackerman, 'Altruism, Nonprofits and Economic Theory,' in Helmut Anheier (ed), *Nonprofit Organisations - Theory, management, Policy* (Routledge, 2005), 126.

¹⁰⁶ A social entrepreneur will create a particular social cause and, in pursuing this cause, will generate innovative process with limited resources. Furthermore, a social entrepreneur will exhibit a sense of accountability towards the constituencies they serve and to their outcome. Gregory Dees, Jed Emerson and Peter Economy, *Enterprising Nonprofits* (John Wiley & Sons, 2001) 126.

¹⁰⁷ Avner Ben-Ner and Theresa Van Hoomissen, 'Nonprofit Organizations in the Mixed Economy' (1991) 62(4) *Annals of Public and Cooperative Economics* 519, 519-550.

¹⁰⁸ Susan Rose-Ackerman, 'Altruism, Nonprofits and Economic Theory' in Helmut Anheier (ed) *Nonprofit Organisations - Theory, Management, Policy* (Routledge, 2005) 126.

¹⁰⁹ Secondary to a not-for-profit organisation's objective and behaviour is the non-distribution constraint of any surplus made. Helmut Anheier, *Nonprofit Organisations - Theory, Management, Policy* (Routledge, 2005) 127.

¹¹⁰ Estelle James, 'The Non-Profit Sector in Comparative Perspective' in W.W Powell (ed) *The Non-Profit Sector: A Research Handbook* (Yale University Press, 1987) 400.

religious ideologies.¹¹¹ Furthermore, this illustrates that not-for-profit organisations choose a mix of services and multiple-products.¹¹²

Where for-profit firms provide a service mix, this is considered to be a managerial decision primarily to maximise profits.¹¹³ However, the decision for a not-for-profit organisation to offer a mix of service is termed a trade-off. A trade-off is found where the not-for-profit organisation's preferred services will not make a sufficient return or revenue to keep that service viable. This requires not-for-profit organisations to be dependent on cross-subsidisation.¹¹⁴ Cross-subsidisation is where a not-for-profit organisation will rely on donations, donated time and efforts (labour) of their members, or volunteers to maintain its preferred services as part of driving the organisation's primary mission.¹¹⁵ These cost inefficiencies suggest a logical question: how can not-for-profit organisations compete with for-profit organisations in the same industry?

Property rights theory answers this question by suggesting that for a not-for-profit to continue operating, it will heavily rely upon the following conditions:¹¹⁶

1. *Entry barriers* – Barriers into a market can be natural or induced by government, but ultimately they do not keep out all competitors. Entry barriers may reduce competition for profit-maximising firms, meaning some will be unable to meet the existing market demand. Not-for-profit organisations will provide services to the residual proportion of the market, which the for-profits cannot serve.
2. *Outside support* – Not-for-profits receive outside support by way of grants, donations and advantage taxation. This kind of support is used to subsidise a not-for-profit's expenditure which will reduce cost inefficiencies.
3. *Scale and scope* – Economies of scale and/or economies of scope allows a not-for-profit organisation to have a higher total cost when compared to a for-profit firm.

¹¹¹ Helmut Anheier, *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 128.

¹¹² Susan Rose-Ackerman, 'Altruism, Nonprofits and Economic Theory', in Helmut Anheier (ed), *Nonprofit Organisations – Theory, Management, Policy* (Routledge, 2005) 126.

¹¹³ Estelle James, 'How Nonprofits Grow: A Model' (1983) *Journal of Policy Analysis and Management* 350, 352.

¹¹⁴ Estelle James, 'How Nonprofits Grow: A Model' (1983) *Journal of Policy Analysis and Management* 350, 352.

¹¹⁵ Benedetto Gui, 'Productive Private Nonprofit Organizations – A Conceptual Framework' (1987) *Annals of Public Cooperative Economy* 415, 418.

¹¹⁶ Daniel Friesner and Robert Rosenman, 'The Property Rights Theory of the Firm and Mixed Competition: A Counter-Example in the US Health Care Industry' (2001) 8(3) *International Journal of the Economics of Business* 437, 438.

4. *Operating objectives* – Reducing cost inefficiencies a not-for-profit organisation should adopt operating objectives, which are similar to for-profit firm.

Despite the cost inefficiencies, a not-for-profit organisation can successfully compete with for-profit organisations by exploiting quality-choice and trade-offs at a lower than normal return. It is found that not-for-profits with operating objectives that coincide with quality and a consumer's price preference may drive for-profits out of the market.¹¹⁷ Another explanation why not-for-profits compete successfully with for-profits is determined by market fundamentals rather than market intervention and regulation.¹¹⁸ Under ordinary cost and demand conditions, for a not-for-profit to increase its production of non-pecuniary benefits, it will enhance a not-for-profit organisation's competing ability. Not-for-profit organisations have a better understanding of the market's needs and are, therefore, capable of adjusting their operating objectives, which results in their increased competitiveness.¹¹⁹

The contribution that the body of economic theories offers is a standardisation that underpins our understanding of how not-for-profits emerge and behave in response to both internal and external forces. These theories show that not-for-profits are a strong economic force in the marketplace – however, economic theory views not-for-profits strictly as economic players within the framework of economic exchange. This view of the not-for-profits overlooks their other unique dimensions, which are also examined in this chapter.

2.5 Not-for-Profit Organisations Through the Lens of Social-Political Theory

Alongside the economists, political scientists and social theorists have also demonstrated an interest in understanding the not-for-profit sector and its organisations; however, the respective focuses of these disciplines differ. Social theorists avail to understand the connection between individuals who create a network (an association) to achieve a benefit for themselves and

¹¹⁷ Daniel Friesner and Robert Rosenman, 'The Property Rights Theory of the Firm and Mixed Competition: A Counter-Example in the US Health Care Industry' (2001) 8(3) *International Journal of the Economics of Business* 437, 446.

¹¹⁸ Daniel Friesner and Robert Rosenman, 'The Property Rights Theory of the Firm and Mixed Competition: A Counter-Example in the US Health Care Industry' (2001) 8(3) *International Journal of the Economics of Business* 437, 438.

¹¹⁹ Daniel Friesner and Robert Rosenman, 'The Property Rights Theory of the Firm and Mixed Competition: A Counter-Example in the US Health Care Industry' (2001) 8(3) *International Journal of the Economics of Business* 437, 447. It should not be overlooked that a shift in operating objectives will be subject to the readily available and immense donative support by way of voluntary labour for this change to take effect.

others.¹²⁰ However, political scientists are concerned with understanding the impact or the contribution a voluntary association has on democratic practices and institutions.¹²¹ Alexis de Tocqueville, the classical social theorist who travelled from France to the United States, was the first to suggest that a not-for-profit organisation enhanced political democracy.

Upon Alexis de Tocqueville's arrival in the United States, he made a number of key observations about civil society.¹²² Relevant to his observations is the historical background of France's treatment of and attitude towards voluntary associations in the nineteenth-century. France's *Penal Code* of 1810 regulated voluntary associations and provided the government with control over an association's purpose and its operation,¹²³ and imposed conditions upon associations as it saw fit.¹²⁴ Tocqueville held concerns about France's political sovereignty over an individual's freedom of association.¹²⁵

Tocqueville's famously stated that the state 'compresses, enervates, extinguishes and stupefies people, till each is reduced to a flock of timid and industrious animals of which the government is the shepherd.'¹²⁶ His remarks emanate from his observations that France's republican model of government was becoming totalitarian and centralised, impacting on an individual's freedom to be involved in public life.¹²⁷ Tocqueville watched France's so-called

¹²⁰ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin, 2001) 204.

¹²¹ Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin 2001) 204–205.

¹²² There is some difficulty in ascertaining a universal definition of civil society. The World Bank defines civil society to mean 'the wide array of non-governmental and not-for-profit organisations that have a presence in public life, expressing interests and the values of their members or others, based on ethical, cultural, political, scientific, religious or philanthropic considerations. Civil society organisations therefore refer to a wide array of organisations: community groups, non-governmental organisations, labor unions, indigenous groups, charitable organisations, faith-based organisations, professional associations and foundations.' World Bank, *Defining Civil Society* (2010)
<<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/CSO/0,contentMDK:20101499~menuPK:244752~pagePK:220503~piPK:220476~theSitePK:228717,00.html>>.

¹²³ Jack Lively, *The Social and Political Thought of Alexis de Tocqueville* (Clarendon Press, 1962) 128.

¹²⁴ A voluntary association could be formed for the purposes of religion and literacy. For associations being formed outside of these purposes, permission from the government was required. The government also imposed conditions on associations not to have more than twenty (20) members and to hold regular meetings. Associations with political and revolutionary purposes would avoid these conditions by dividing into groups of less than twenty (20) and not hold regular meetings. Jack Lively, *The Social and Political Thought of Alexis de Tocqueville* (Clarendon Press, 1962) 128.

¹²⁵ Jack Lively, *The Social and Political Thought of Alexis de Tocqueville* (Clarendon Press 1962) 128.

¹²⁶ Alexis de Tocqueville, *Democracy in America* (1835-1840) 2, 319 in Robert Holton and Bryan Turner (eds) *Classical Social Theory, The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 38.

¹²⁷ Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 37.

model of democracy encourage privatism, which inhibited an individual's participation in politics.¹²⁸ The political action was judged in terms of an individual's private advantage over the wider public interest.¹²⁹ According to de Tocqueville, this privatism discouraged the formation of political associations, and he held grave concerns about the future of France's democracy.¹³⁰

However, when de Tocqueville travelled to the United States, he observed a different political sovereignty to that of the centralised government of France. Tocqueville noticed that America's political structure actively encouraged political participation through citizenship rights and education.¹³¹ He saw individuals were motivated to form voluntary associations, which permitted every kind of opinion and grievance to be expressed.¹³² Building the connection between voluntary associations and democracy, Tocqueville observed that creating a voluntary association was not an easy task. However, within a democracy, an association will thrive when certain conditions are present.¹³³ These conditions, which Tocqueville identified, are: (i) a free press; (ii) the freedom to be self-organised; and (iii) the freedom to be self-reliant.¹³⁴ While identifying these predominate conditions, Tocqueville also saw voluntary organisations were independent, autonomous, and free from state control.¹³⁵ Tocqueville's historical milestone of pointing out the connection between voluntary associations and a vibrant democracy has influenced many other theorists.

Civil society theorists argue that a citizen's involvement with an intermediate organisation enhances democracy.¹³⁶ These intermediate organisations are identified as being smaller than

¹²⁸ Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 37.

¹²⁹ Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 37-38.

¹³⁰ Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 38.

¹³¹ Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 38.

¹³² Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 38.

¹³³ Lively, Jack, *The Social and Political Thought of Alexis de Tocqueville* (Clarendon Press, 1962) 130.

¹³⁴ Lively, Jack, *The Social and Political Thought of Alexis de Tocqueville* (Clarendon Press, 1962), 130.

¹³⁵ Robert Holton, 'Classical Social Theory' in Bryan Turner (ed), *The Blackwell Companion to Social Theory* (Blackwell Publishers, 1997) 37.

¹³⁶ Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 866. See also Jürgen Habermans, *The Structural Transformation of the Public Sphere* (Polity Press, 1992); Jude Howell and Jenny Pearce, *Civil Society & Development. A Critical Interrogation* (Boulder, 2002); Mary Kaldor, *Global Civil Society: An Answer to War* (Polity Press, 2003).

government, but larger than individual families.¹³⁷ These organisations function as a mediating structure between an individual's private sphere and the state.¹³⁸ Within this space individuals will have a meaningful relationship and a dialogue with the state that they would not necessarily have on their own.¹³⁹ Additionally, an individual's level of political participation is influenced by an organisation's environment.¹⁴⁰ The environment of a not-for-profit organisation is credited for building norms of reciprocity, cooperation and trust between members, which generates social capital.¹⁴¹

Sociologist James Coleman describes social capital as the glue that binds the norms of trust and reciprocity, and which facilitates cooperative arrangements between members of a not-for-profit organisation.¹⁴² Trust is the essential component of social capital, for it is the moral source that underpins the collective action by members to solve a problem.¹⁴³ Advancing the notion of social capital is Robert Putnam, who asserted that social capital also serves as the connection to a strong civil society, which builds and drives a successful democratic government.¹⁴⁴ A successful democracy, according to Putnam, depends on citizens voting, a belief that others will vote, and citizens showing their preferences by participating in non-voting activities.¹⁴⁵ Civic participation or engagement¹⁴⁶ is important to democracy, for it allows citizens to influence (or at least try to

¹³⁷ Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 867.

¹³⁸ Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 867.

¹³⁹ Resulting from the complexity and vastness of the state and big business an individual can find it impossible (or at least impossible) to engage with the state. Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 867.

¹⁴⁰ Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 867.

¹⁴¹ Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 867.

¹⁴² J. S. Coleman, 'Social Capital in the Creation of Human Capital' in Mark Lyons, *Third Sector – The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Allen & Unwin, 2001) 207.

¹⁴³ Dana Brakman Reiser, 'Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits' (2003) 82 *Oregon Law Review* 829, 896.

¹⁴⁴ Putnam, Robert, *Making Democracy Work: Civic Traditions in Modern Italy* (Princeton University Press, 1993) 83–16.

¹⁴⁵ Putnam, Robert, *Making Democracy Work: Civic Traditions in Modern Italy* (Princeton University Press, 1993) 167–170.

¹⁴⁶ Civic engagement means any collective action by individuals to improve our society. This may be achieved through learning about our political system, issues of the day and acting on concerns through voluntary and community organisations. Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermine Citizen Participation and What we can do about it* (Brookings Institute Press, 2005) 6–7.

influence) government activity.¹⁴⁷ However, internal and external forces shape an individual's ability and willingness to participate in a democracy and in an association.¹⁴⁸

Internal forces are considered to be the resources that citizens have at their disposal, such as their time, skill and money.¹⁴⁹ In contrast, external forces are the social circumstances in which individuals may find themselves. For instance, some individuals will live in a community where they are expected to participate.¹⁵⁰ Likewise, there are individuals who possess strong feelings of community in the area where they live.¹⁵¹ Having a sense of belonging to a community provides a network for individuals to become involved in political affairs.¹⁵² These networks have found to be positive norms of reciprocity, which encourages and reinforces civic participation, but it is not always the case.¹⁵³ Examples of the downside of social capital include the Ku Klux Klan and the Oklahoma City Bomber, Timothy McVeigh.¹⁵⁴ Social capital enabled McVeigh to build a network of friends to form a conspiracy that bound them together by a norm of reciprocity.¹⁵⁵ Besides informal networks, formal organisations also afford a citizen the opportunity to participate through collective action.¹⁵⁶

Sociologist, Roger Lohmann, holds the view that associations have a role in public action. Lohmann states that associations allow a specific group of people to come together to speak about their common situation and act on it through the power they generate.¹⁵⁷ The power

¹⁴⁷ Sidney Verba and Norman H. Nie, *Participation in America Political Democracy and Social Equality* (University of Chicago Press, 1972) 8.

¹⁴⁸ Sidney Verba and Norman H. Nie, *Participation in America Political Democracy and Social Equality* (University of Chicago Press, 1972) 13.

¹⁴⁹ Sidney Verba and Norman H. Nie, *Participation in America Political Democracy and Social Equality* (University of Chicago Press, 1972) 13.

¹⁵⁰ Sidney Verba and Norman H. Nie, *Participation in America Political Democracy and Social Equality* (The University of Chicago Press 1972), 13.

¹⁵¹ Christine Kelleher and David Lowery, 'Political Participation and Metropolitan Institutional Context' (2004) 39 *Urban Affairs Review* 728.

¹⁵² Christine Kelleher and David Lowery, 'Political Participation and Metropolitan Institutional Context' (2004) 39 *Urban Affairs Review* 728.

¹⁵³ Robert Putnam, *Bowling Alone – The Collapse and Revival of American Community* (Simon & Schuster, 2000) 21.

¹⁵⁴ Robert Putnam, *Bowling Alone – The Collapse and Revival of American Community* (Simon & Schuster, 2000) 21.

¹⁵⁵ Robert Putnam, *Bowling Alone – The Collapse and Revival of American Community* (Simon & Schuster, 2000) 21.

¹⁵⁶ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What we can do about it* (Brookings Institute Press, 2005) 67.

¹⁵⁷ Roger Lohmann, *The Commons: New Perspectives on Nonprofit Organizations and Voluntary Action* (Jossey-Bass, 1992) 172-175.

generated by this public action encourages the creation of associations.¹⁵⁸ However, the level of an individual's participation in voluntary associations (being both social and political) are directly linked to an individual's level of education.¹⁵⁹

It has been shown by Putnam that individuals with a high level of education are likely to be more involved in organisations that are concerned with public affairs and politics.¹⁶⁰ Conversely, it has been found that individuals with a lower level of education are members of voluntary organisations, usually religious groups.¹⁶¹ Individuals with a low level of education participate in voluntary organisations to gain experiences to develop their civic skills such as, communication.¹⁶² Putnam explains that education is indicative to an individual's level of participation in civil society mainly because education is the proxy for social status and economic differences.¹⁶³

When social status and economic differences are combined with the individual's income, it is predicted that well-educated individuals will tend to be trusting¹⁶⁴ and be joiners.¹⁶⁵ This is partly because education, and to some degree the individual's home life, impart the necessary skills and resources for civic participation.¹⁶⁶ For example, highly educated people are more likely use their communication skills to write to office holders, join a campaign and attend local political meetings,¹⁶⁷ and are active in voluntary associations.¹⁶⁸ Furthermore, it is found that individuals

¹⁵⁸ William W. Clohesy, 'Fundraising and the Articulation of Common Goods' (2006) 32 *Nonprofit and Voluntary Sector Quarterly* 128,132.

¹⁵⁹ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect*, 34, 36.

¹⁶⁰ Gabriel A. Almond and Sidney Verba, *The Civic Culture – Political Attitudes and Democracy in Five Nations* (Princeton University Press, 1963) 304-305.

¹⁶¹ Gabriel A. Almond and Sidney Verba, *The Civic Culture – Political Attitudes and Democracy in Five Nations* (Princeton University Press, 1963) 304.

¹⁶² Sidney Verba, K. Scholozman and H. Brady, *Voice and Equality: Civic Voluntarism in American Politics* (Harvard University Press, 1995) 519.

¹⁶³ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34, 36. The data shows that fifty per cent (50%) of manual workers are excluded from voting. David McKay, *American Politics and Society* (Wiley-Blackwell, 7th ed, 2009) 120.

¹⁶⁴ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34, 36-37.

¹⁶⁵ Arther Schlesinger Sr in 1944 called the United States of America a 'nation of joiners'. Marc Howard, 'American Civic Engagement in Comparative Perspective' (2006) 2(3) *Democracy & Society* 16, 17.

¹⁶⁶ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34, 37.

¹⁶⁷ Steven Rosenstone and John Hansen, *Mobilization, Participation and Democracy in America* (Macmillan, 1992) 74.

¹⁶⁸ Sidney Verba, Kay Scholozman, Henry Brady and Norman Nie, *Voice and Equality: Civic Voluntarism in American Politics* (Harvard University Press, 1995) 353.

who are civically engaged will be five times more likely to protest than those individuals who are not.¹⁶⁹ Evidence has emerged that social capital and civic engagement has declined.¹⁷⁰

Robert Putnam has charted the decline of civil participation in the United States of America since the 1950s.¹⁷¹ Putnam measures the decline of civic engagement by the level of voter turnout and electoral participation, such as protesting.¹⁷² Explaining the decline of civic participation in the United States, Putnam has identified three factors: (i) personal – characteristics of the individual voter; (ii) structural – those characteristics of the American political system; and (iii) cultural – characteristics that reflect society and culture in America.¹⁷³ Each factor will be discussed individually.

(i) Personal

Personal factors diminishing civic engagement are twofold. First is the deterioration of civic and government courses in American high school curricula.¹⁷⁴ By taking away traditional classroom-based civic education, has been found to have a negative impact on an individual's political knowledge¹⁷⁵ and quality of participation.¹⁷⁶ Since World War II, levels of education have improved; however, it has been found that having a better-educated individual does not necessarily correlate to high levels of civic engagement.¹⁷⁷

Secondly, an individual's regular use of newspaper and radio has been identified as a personal factor linked to civic participation.¹⁷⁸ The decline of individuals reading newspapers, watching

¹⁶⁹ Russell Dalton, 'The Two Faces of Citizenship' (2006) 2(2) *Democracy & Society*, 16, 22.

¹⁷⁰ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34.

¹⁷¹ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34.

¹⁷² Russell Dalton, 'The Two Faces of Citizenship' (2006) 2(2) *Democracy & Society* 16, 22.

¹⁷³ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 31-32.

¹⁷⁴ Since the 1970s, American high schools have reduced their civic and government courses by two-thirds. Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 33.

¹⁷⁵ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 33.

¹⁷⁶ William Galston, 'Political Knowledge, Political Engagement, and Civic Engagement' (2001) 4 *Annual Review of Political Science* 217, 219.

¹⁷⁷ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 32.

¹⁷⁸ William Galston, 'Political Knowledge, Political Engagement, and Civic Engagement' (2001) 4 *Annual Review of Political Science* 217, 222.

the nightly news, and staying informed through traditional means has resulted in a generation of individuals that are not as politically attentive or aware as earlier generations.¹⁷⁹

(ii) *Structural*

Structural characteristics are also been recognised as contributors to the decline of civic engagement. These have been identified as the media and the nature of electoral system itself. The media environment and the role it plays in the electoral process have people becoming disengaged with politics, and this has influenced the level of media coverage of elections and other political events.¹⁸⁰ For instance, the major news networks in America only covered four and a half hours of the fall elections in 2000, compared to six hours and twenty minutes in 1992.¹⁸¹ Despite this disengagement, there are more media outlets, such as cable and the Internet, which people can access. However, it is found that only interested persons are motivated to seek out political news through these media outlets.¹⁸² The media is not alone in contributing to the decline of civic participation – there are also the activities that transpire within the electoral system.

The lack of voter turnout has been blamed on voter fatigue.¹⁸³ American voters have lost interest in the campaigning process and have reported to be fatigued by what seems to be ongoing electioneering.¹⁸⁴ Another factor influencing poor voting turn out is the lack of political mobilisation. This involves targeting particular individuals or a group of individuals to mobilise their support.¹⁸⁵ Traditionally, voluntary organisations such as the parent-teachers associations, fraternal groups, and professional organisations would mobilise their members to vote. However, declining membership within these organisations has seen political parties now undertake voter

¹⁷⁹ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 33.

¹⁸⁰ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 41-42.

¹⁸¹ Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 42.

¹⁸² Those interested persons are also referred to as ‘political junkies’. Stephen Macedo et al, *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 42, 44.

¹⁸³ Since 1960, the number of Americans turning out to vote for presidential campaigns is now at fifty-five per cent (55%) and fifty per cent (50%) for congressional campaigns. For the 1996 presidential campaign, there was only a 48.4 per cent turn out, which was the lowest since 1924. In 2000, fifty-one per cent (51%) turned out and figures bounced up to sixty-nine per cent (69%) in 2008. However, state and local elections show only a twenty per cent (20%) turn out. David McKay, *American Politics and Society* (Wiley-Blackwell, 7th ed, 2009) 117–118.

¹⁸⁴ David McKay, *American Politics and Society* (Wiley-Blackwell, 7th ed, 2009) 117-118.

¹⁸⁵ Stephen Macedo et al, *Democracy at Risk: How Political Choices Undermines Citizen Participation, and What We Can Do About It* (Brookings Institute Press, 2005) 437.

mobilisation.¹⁸⁶ Political parties have been found to structure their mobilisation strategy towards their ‘faithful’ supporters, which excludes the young, the poor and immigrants.¹⁸⁷ Against a backdrop of having no civic education in schools, and with particular societal groups excluded from the political network, civic participation will remain in free-fall and in a state of disarray. Underpinning this state of decline is a number of cultural factors that also impact on the level an individual’s civic participation.

(iii) Cultural

The factor of interpersonal trust has been previously identified as a link to an individual’s level of participation and engagement in civil society.¹⁸⁸ Participation is driven not by an individual’s own level of trust, but rather the level of personal trust which surrounds the individual.¹⁸⁹ Voluntary associations are integral to social capital in democratic societies, and they allow individuals to participate in a meaningful way to community life.¹⁹⁰

Although Salamon states that there has been a surge in the creation of voluntary associations, describing this phenomenon as a ‘global associational revolution’,¹⁹¹ participation in associational life is steadily declining. Both Australia and the United States have recorded sharp declines over the past forty years in the development of and the level of participation in a not-for-profit organisation.¹⁹² Australia’s deterioration in associational life is reflected in the average number of hours an individual volunteered to a not-for-profit organisation. Data indicates that the median hours provided by volunteers in community and welfare services has fallen from 48 hours to 40 hours between 2000 and 2006.¹⁹³ In the same period, the largest fall in voluntary hours was

¹⁸⁶ Stephen Macedo et al, *Democracy at Risk: How Political Choices Undermines Citizen Participation, and What We Can Do About It* (Brookings Institute Press, 2005) 437–48.

¹⁸⁷ Stephen Macedo et al, *Democracy at Risk: How Political Choices Undermines Citizen Participation, and What We Can Do About It* (Brookings Institute Press, 2005) 48.

¹⁸⁸ Stephen Macedo et al., *Democracy at Risk: How Political Choices Undermines Citizen Participation, and What We Can Do About It* (Brookings Institute Press, 2005) 50.

¹⁸⁹ Stephen Macedo et al., *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 50.

¹⁹⁰ Stella Minahan and Loretta Inglis, ‘Organisational Decline and Renewal in an Australian Voluntary Association’ (Working Paper Series No 2/08, Monash University, February 2008) 1.

¹⁹¹ Lester Salamon, ‘The Rise of Nonprofit Sector’ 73(4) *Foreign Affairs* (1999) 109.

¹⁹² Stephen Macedo et al., *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 50; Stella Minahan and Loretta Inglis, ‘Organisational Decline and Renewal in an Australian Voluntary Association’ (Working Paper Series No 2/08, Monash University, February 2008) 1.

¹⁹³ Productivity Commission, ‘Contribution of the Not-for-Profit Sector’ (Research Report, Productivity Commission, January 2010) 70.

recorded for religious organisations, where the medium hours fell from 60 hours to 48 hours.¹⁹⁴ Little is known about what causes the decline of participation in voluntary associations in Australia.¹⁹⁵ However, substantial research has been undertaken in America to explain the decline in associational life and in civic participation.

Another factor identified as correlating to the demise of social engagement is television watching.¹⁹⁶ According to Putnam, television viewing has a negative impact on social trust, which reduces individuals' participation in social, recreational and community activities, and connection to their neighbourhoods.¹⁹⁷ Past generations had strong neighbourhood and local bonds due to moral and religious doctrines.¹⁹⁸ In contemporary society, individualism has also been identified as the dynamic shift in America's public culture and the main contributor to the decline of civic participation.

The dominant cultural norm of individualism turns civic engagement into a choice for an individual rather than a responsibility.¹⁹⁹ Voting, which is non-compulsory in America, sees individuals undertaking a cost-benefit analysis on whether or not it is worth it to vote.²⁰⁰ An individual's decision to vote or not is determined by the costs related to the exercise of voting against any benefit the individual will receive from the exercise.²⁰¹ Poor voter turnout, also, explains the change in campaigning and policy by the main political parties.

The Democratic Party (the Democrats) has shown its willingness to shift away from traditional class-based politics and engineered its election campaigns to focus on issues of the day

¹⁹⁴ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 70.

¹⁹⁵ Stella Minahan and Loretta Inglis, 'Organisational Decline and Renewal in an Australian Voluntary Association' (Working Paper Series No 2/08, Monash University, February 2008) 2; T. M Dacin and W.R Scott, 'Institutional Theory and Institutional Change: Introduction of the Special Research Forum' (2002) 45(1) *The Academy of Management Journal* 45; D. Whetten, 'Growth and Decline Processes in Organisations' (1987) 13 *Annual Review of Sociology* 335.

¹⁹⁶ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34, 46.

¹⁹⁷ Robert Putnam, 'The Strange Disappearance of Civic America' (1996) 24 *The American Prospect* 34, 46–48.

¹⁹⁸ Stephen Macedo et al., *Democracy at Risk: How Political Choices Undermines Citizen Participation, and What We Can Do About It* (Brookings Institute Press, 2005) 51.

¹⁹⁹ Stephen Macedo et al., *Democracy at Risk: How Political Choices Undermines Citizen Participation, and What We Can Do About It* (Brookings Institute Press, 2005) 51.

²⁰⁰ Stephen Macedo et al., *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 51–52.

²⁰¹ Stephen Macedo et al., *Democracy at Risk – How Political Choices Undermines Citizen Participation and What We Can Do About It* (Brookings Institute Press, 2005) 51–52.

and the candidate.²⁰² One of the election issues in the 2008 Presidential Campaign was wealth inequalities and economic dislocation. Addressing these inequalities, and to motivate individuals to vote for the Democrats, they promised income redistribution through taxation and to increase federal spending.²⁰³ The success of the Democrats 2008 presidential campaign achieved a renewal in civic participation, but their campaign's real success lies in the well-crafted policy that promised gains or benefits for individuals.²⁰⁴

Finally, it has been demonstrated that not-for-profit organisations are an integral mediatory structure between the community and the state. These associational structures are the mechanisms that permit groups of individuals to work collectively and to participate in civil society. Civic participation is influenced by social capital, wherein these groups are social networks connected by trust and norms of reciprocity. The decline of civic engagement in the United States is largely due to the structure of the American political system, the reduction of civic courses in formal schooling, and a cultural shift towards individualism. To avoid further erosion of social capital and civil society, it is critical that not-for-profit organisations strengthen their position in the civic landscape.

2.6 Conclusion

Debate surrounding which term is the most appropriate to accurately describe the sector across jurisdictions has led to the development of a universal definition and classification of the sector. The core of this universal definition and the classification system was to provide clarity that will overcome the sometimes-blurred boundaries of other economic units, such as the state, households, and for-profit units. The structural-operational definition provides key characteristics that are the hallmarks of a not-for-profit organisation, and the classification system developed a measuring framework that captures data about not-for-profit organisations' activities and outputs.

Understanding the not-for-profit sector and its organisations' economic theory addresses why the sector exists. Economists believe they exist to address market failure, and non-rival goods, such as national defence, cannot be produced by a private firm and, therefore, can only be

²⁰² David McKay, *American Politics and Society* (Wiley-Blackwell, 7th ed, 2009) 120.

²⁰³ David McKay, *American Politics and Society* (Wiley-Blackwell, 7th ed, 2009) 120.

²⁰⁴ David McKay, *American Politics and Society* (Wiley-Blackwell, 7th ed, 2009) 120.

produced by the state through taxation. The state will provide other particular goods with the aim of satisfying the medium voter, but when consumers are unsatisfied, they will turn to not-for-profit organisations. Consumers view not-for-profit organisations as trustworthier than for-profits and, therefore, are willing to support them. Contributing to a not-for-profit organisation's trustworthiness is the non-distribution constraint principle, which trumps opportunistic behaviour found in for-profits.

Entrepreneurship theory states a not-for-profit organisation will provide a mixture of services. Providing a mixture of services is not always viable for these organisations but, despite the cost inefficiencies, a not-for-profit can successfully compete with for-profits. The success of a not-for-profit organisation in these circumstances relies on cross-subsidisation.

Superfluous to a nation's gross domestic product, the not-for-profit sector and its organisation are important to democracy. Alexis de Tocqueville had observed during his travels to the United States that citizens formed voluntary associations, which enhanced political democracy. Tocqueville further observed that voluntary associations would thrive in an environment with a free press and the freedom to be self-organised and self-reliant.

Voluntary associations have been found to provide an environment for individuals to build norms and general social capital. Putnam asserts that social capital is the connection to building a strong democratic government, but this is reliant on citizens voting and other means of civic participation. The level at which individuals will engage in civic activities (such as signing petitions) is largely influenced by their level of education, resources at their disposal, and their social circumstances.

However, in more recent times, civic participation has declined both in Australia and the United States. The factors linked to the decline in civic participation are election fatigue and the dominant cultural norm of individualism. This is the challenge for not-for-profit organisations to strengthen their place in the civic landscape.

CHAPTER 3: History of Incorporated Associations in Australia and New Zealand

*Our sector has steadily grown in size and influence by harnessing the spirit of community and the benevolent instincts of human nature.*²⁰⁵

3.0 Introduction

This chapter outlines the creation of the incorporated association model in South Australia, and the motivating needs for a simple form of incorporation for charitable institutions. This new organisational form was innovative for its time, and the structure of an incorporated association was slowly adopted by the other Australian jurisdictions.

The South Australian model of incorporation has been much celebrated as pioneering; however, it is New Zealand's model of incorporation that has had a lasting impact. Chapter Three examines the development of New Zealand's *Incorporated Societies Acts* in juxtaposition with the South Australian *Associations Incorporation Act 1858*. This examination found particular aspects of New Zealand's incorporated model were more advanced than South Australia's, and these features will be highlighted in this chapter. Sir John Salmond can be accredited as the person responsible for shaping these advances, which the South Australian parliament subsequently adopted. Chapter Three briefly discusses the influence Salmond's juristic theories had in developing New Zealand's model of incorporation.

3.1 History of Incorporated Associations in Australia

The introduction of incorporated association legislation originated in South Australia, and the state was acclaimed as the leader in the development of association law for all Australian jurisdictions.²⁰⁶ The South Australian parliament enacted two momentous pieces of legislation in 1858: the *Real Property Act 1858*; and the *Associations Incorporation Act 1858*.²⁰⁷ The primary

²⁰⁵ Private Action, Public Benefit. A Review of Charities and Wider Not-for-Profit Sector, Strategy Unit Report. September 2002, 5.

²⁰⁶ A.S. Sivers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 93.

²⁰⁷ Compared to the *Real Property Act 1858* (SA), the *Associations Incorporation Act 1858* (SA) took longer for other Australian jurisdictions to enact incorporation association statute.

aim of the latter statute was to offer a simple and cheap method of incorporating a non-profit organisation established for a specific community purpose.²⁰⁸ However, the enactment of the *Associations Incorporation Act* was neither trouble-free nor simple.²⁰⁹

The need for an appropriate incorporated entity for not-for-profit institutions in Australia was due to a number of practical and legal difficulties experienced by not-for-profit associations. As is the case today, the courts did not recognise the existence of an association or, more accurately, an unincorporated association.²¹⁰ The only way this issue could be overcome was through either incorporating under the company's legislation of the day, or to create a charitable trust.²¹¹ The trust deed became a challenge for non-profit associations when it came to managing their real property. The property was vested in trustees and not in an association's name, and every time there was a change of a trustee, there was an expense for the association to transfer the association's property to a newly appointed trustee.²¹² To overcome this core problem, the South Australian Parliament undertook the legislative development to incorporate associations to save time and money.²¹³

Captain Bagot MLC first tabled the *Bill for the Associations Incorporation Act* in the Legislative Council on 21 January 1858.²¹⁴ This Bill proposed a scheme of incorporation through the granting of a certificate by the Master of the Court, creating a means for an association to hold property in its own name.²¹⁵ Pursuant to the Bill, incorporation could only extend to certain prescribed organisations:

1. churches;
2. schools;

²⁰⁸ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224.

²⁰⁹ 1858 (SA).

²¹⁰ *Leahy v Attorney-General of New South Wales* (1959) 101 CLR; *John v Rees* [1970] Ch 345.

²¹¹ Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 207.

²¹² Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 207; Captain Bagot, Preamble to Act No. 21 of 1858 (SA) in Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 208.

²¹³ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 225.

²¹⁴ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 207 n 2.

²¹⁵ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 225.

3. hospitals;
4. benevolent and charitable institutions;
5. mechanics' institutions; and
6. any other institution that promoted science, the arts, and literature.²¹⁶

The Bill is celebrated for its uniqueness, as there was no British precedent on which it could directly or indirectly base itself.²¹⁷ The most significant features of the Bill were: that it allowed for existing associations to amend their rules to become incorporated; and, secondly, ensured the vesting of personal and real property in a newly formed self-managing corporation.²¹⁸

However, the Bill had some limitations as it did not provide for members' rights, nor confer limited liability on members; this, consequently, meant members were personally liable for an association's debts.²¹⁹ Following the Bill being introduced by Captain Bagot MLC to the Legislative Council on 21 January 1858, the Bill lapsed.²²⁰ It was re-introduced into the South Australian Parliament in September that year by Captain Bagot MLC.²²¹ There were no changes to the Bill on its re-introduction.²²² During its progress, albeit slow, discussions about the Bill in both houses of parliament emphasised the need for not-for-profit institutions to become

²¹⁶ Associations Incorporation Bill 1857(SA) cl 9 in Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 225.

²¹⁷ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 225.

²¹⁸ *Associations Incorporation Act 1858* (SA) ss 5–6.

²¹⁹ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 225–226.

²²⁰ Captain Bagot is acclaimed for creating the incorporation association structure by introducing the Bill. However, he was not the drafter of the Bill. This was someone, described by Captain Bagot, as a member of the legal profession and of 'considerable eminence'. Captain Bagot's role in the creation of the incorporated association is that of a parliamentary agent – nevertheless, this role should not be underestimated, because he had the fortitude to pursue the Bill and the insight to understand the troubles facing charities at that time. Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 226. It is Taylor's view that AJ Mann was responsible for the creation of the incorporated association. Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 225–226.

²²¹ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 226.

²²² Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 208.

incorporated for effective and efficient property management – the Bill finally received Royal Assent on 24 December 1858.²²³

3.2 Troubles for South Australia's *Incorporated Associations Act*

The life of this pioneering Act was short lived, and it was repealed in 1864 by South Australia's *Companies Act 1864*.²²⁴ It is not entirely clear why the *Companies Act 1864* (SA) repealed the association's incorporation legislation; however, one explanation provided is that in the 19th century there were tensions in the role of colonial legislators either to be innovative law reformers or mere transmitters of English law.²²⁵ Innovation was placed on hold in South Australia with the passing of the *Companies Act 1864* (SA), which was a direct reprint of the English Act.²²⁶ Over time, the repealing of the association's incorporation legislation has proved to be a mistake.

Within a short period, the *Companies Act 1864* (SA) showed that it was too complex and an expensive means of incorporation for not-for-profit entities.²²⁷ To the credit of the South Australian Parliament, it realised that it already had an appropriate and suitable structure for not-for-profit entities. Subsequently, Captain Bagot's Act was revived in 1865. However, over time, the Act has been amended and consolidated on numerous occasions. Table 4 shows the lifecycle of South Australia's association incorporation legislation.²²⁸

²²³ Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 208-209 nn4-5; Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 209.

²²⁴ Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 210.

²²⁵ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* (2002-2003) 224, 233.

²²⁶ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 233.

²²⁷ The inadequacy of the corporation legislation was seen through the Port Adelaide Grammar School. Pursuant to the *Companies Act 1864* (SA) it was presumed that the Grammar School would make a profit and its investors would be safeguarded, but all the Grammar School wanted was incorporation, and as the school was affiliated to a Church the *Companies Act 1864* (SA) failed to meet the needs of a not-for-profit organisation. Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 233-234.

²²⁸ *Associations Incorporation Act (No. 12) 1865* (SA) in Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 210 and Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 234.

Table 4 – The lifecycle of South Australia's *Incorporated Association Legislation*

Year	Title	Notable Features / Amendments
1858	<i>Associations Incorporation Act 1858</i> (SA)	<ul style="list-style-type: none"> Allows for the incorporation of not-for-profit institutions. Allows an institution to hold property and to apply the property to the organisation's purpose. Internal management of the organisation was at the members' discretion.
1865	<i>Associations Incorporation Act (No 12) 1865</i> (SA)	<ul style="list-style-type: none"> Referred to as the <i>Revival Act</i>.²²⁹ No changes.
1887	<i>Associations Incorporation Act 1865</i> (SA)	<ul style="list-style-type: none"> Associations permitted to mortgage their property.²³⁰
1890	<i>Associations Incorporation Act 1890</i> (SA)	<ul style="list-style-type: none"> Consolidation.²³¹ Allowed an incorporated association to change its name.²³² Removed the requirement for applicants to advertise for incorporation.²³³
1897	<i>Associations Incorporation Act 1890, Amendment Act 1897 (No. 678) 1879</i> (SA)	<ul style="list-style-type: none"> Every association incorporated under the <i>Associations Acts</i> of 1858, 1887 and 1890 was declared to be an association within the meaning of section 109 of the <i>Companies Act 1892</i> (SA).²³⁴
1901	<i>An Act to amend the Associations Incorporation Act 1890, Amendment Act 1897 (No. 757) 1901</i> (SA)	<ul style="list-style-type: none"> Incorporated associations under the 1858 and 1890 Acts were declared to be an association under section 189 of the <i>Companies Act 1892</i> (SA).²³⁵
1919	<i>Associations Incorporation Act Further Amendment Act 191 No. 1376 1919</i> (SA)	<ul style="list-style-type: none"> The definition of association is amended to include the word 'promoting' before the words 'recreation and amusement'.²³⁶
1929	<i>Associations Incorporation Act 1929</i> (SA)	<ul style="list-style-type: none"> Re-introduced an intention to be incorporated must be advertised.²³⁷ Penalties for seal holders who failed to notify of any changes to an association's name, membership, rules and regulations.²³⁸ Registrar to cancel registration if an association was found to be carrying on trade or if an association is defunct.²³⁹

²²⁹ Greg Taylor, 'The Origins of Associations Incorporation Legislation – The Associations Incorporation Act 1858 of South Australia' (2002-2003) 22 *University of Queensland Law Journal* 224, 233-234.

²³⁰ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 210 n 15.

²³¹ Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 210.

²³² Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 210

²³³ Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 210.

²³⁴ s 5.

²³⁵ s 2.

²³⁶ s 3.

²³⁷ s 4.

²³⁸ s 13.

²³⁹ ss 14–15.

1956	<i>Associations Incorporation Act 1929 (SA)</i>	<ul style="list-style-type: none"> • The Registrar of Companies to hear objections for incorporation instead of the Supreme Court.²⁴⁰ • Appointment of a public officer replaces seal-holders.²⁴¹ • Amalgamation and dissolution of associations permitted.²⁴² • Limited liability provided to members of an association.²⁴³
1985	<i>Associations Incorporation Act 1985 (SA)</i>	<ul style="list-style-type: none"> • Current legislation. • See Part 6 for the Act's legislative history.²⁴⁴

From the inception of this Act, it appears that many of its amendments, outlined above, correspond to particular aspects of New Zealand's model of incorporation – this is also evident in other Australian jurisdictions.²⁴⁵

3.3 Other Australian States

The rest of Australia initially disregarded South Australia's model of incorporation and went about constructing their own efforts to remedy the problems of unincorporated associations. Table 5 is a chronology of when Australian jurisdictions enacted incorporated association legislation.

Table 5 – Chronology of incorporated association statutes

State or Territory	Year
Western Australia	1895
Australian Capital Territory	1953
Northern Territory	1963
Tasmania	1964
Victoria	1981
Queensland	1981
New South Wales	1984

Despite the importance of this legal structure and its legislation, the states and territories have failed to continue along this innovative path.²⁴⁶ This failure ignores the needs and demands that not-for-profit organisations face in contemporary Australia, such as the need to create a modern

²⁴⁰ ss 7–8.

²⁴¹ s 15.

²⁴² s 28.

²⁴³ s 29.

²⁴⁴ South Australia's current associations legislation has been amended on numerous occasions, dating back to 1992.

²⁴⁵ See 3.4 of this thesis for a History of New Zealand's Incorporation model of Non-Profits.

²⁴⁶ Creating new forms for not-for-profit entities was undertaken in the United Kingdom. See Chapter Seven of this thesis for a discussion of innovative not-for-profit entities found in the United Kingdom's not-for-profit sector.

definition of ‘charity’.²⁴⁷ Chapter Six of this thesis identifies and addresses areas within the sector that are in urgent need of reform. Many Australian state and territories were slow in implementing their own associations legislation; however, when it came to devising their incorporation model, they did not necessarily copy South Australia, but took elements from New Zealand’s incorporation model.

3.4 History of New Zealand’s Incorporation Model for Non-Profits

In 1895, New Zealand’s parliament passed the *Unclassified Societies Registration Act* (‘the *Unclassified Societies Act*’).²⁴⁸ Not unlike the South Australian position, the primary object of this Act was to address the ‘unsatisfactory position’²⁴⁹ that clubs and other associations found themselves in by having no legal status.²⁵⁰ Members of various clubs and associations complained that they had no voice or control, and trustees were doing whatever they desired with the associations’ monies.²⁵¹ Less restrictive than the South Australian Act, the *Unclassified Societies Act 1895* (NZ) allowed *any* [my emphasis] group or association to be incorporated provided that: (i) it was formed for any lawful purpose that was not for a pecuniary gain; and (ii) there was to be no less than fifteen members.²⁵² Although the aim of the South Australian and New Zealand parliaments was to remedy the troubles connected with the management of an unincorporated association’s property, aspects of the New Zealand Act offered more than the South Australian model of incorporation in some areas.

²⁴⁷ Standing Committee on Economics, Parliament of Australia, *Inquiry into the Definition of Charities and Related Organisations* (June 2011) 71–75.

²⁴⁸ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 221.

²⁴⁹ New Zealand, *Parliamentary Debates*, 1895, 90 N.Z.P.D. 553 (Sir P. A. Buckley, Attorney-General) in Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 215–216.

²⁵⁰ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 215.

²⁵¹ New Zealand, *Parliamentary Debates*, 1895, 90 N.Z.P.D. 553 (Sir P. A. Buckley, Attorney-General) in Fletcher, Keith, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 216. Members of the unincorporated associations would fear that Trustees might abscond with the club’s funds. Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 16–17.

²⁵² Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 216. Prior to the passing of the *Unclassified Societies Act 1895* (NZ) the company’s legislation recognised unincorporated and non-profit associations (along with partnerships) as a non-commercial enterprise. However, the category of non-commercial enterprises did not extend to nor legally recognise special associations or voluntary groups. Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 11–13A.

The incorporation process under the *Unclassified Societies Act 1895* (NZ) was simple, as it excluded the requirement of advertising and, moreover, provided members with limited liability.²⁵³ While South Australia removed the need to advertise for incorporation in 1890,²⁵⁴ it did not introduce member's limited liability until 1956. Additional innovative features that the South Australian legislation lacked were the ability for an organisation to be voluntarily dissolved, and the requirement for an organisation to have a registered office.²⁵⁵ Further, the *Unclassified Societies Act* (NZ) in 1906 was amended to require associations to file a set of rules with their application for registration.²⁵⁶ These amendments provided a Schedule outlining matters that an association's rules were required to address:

- a) the Society's Name;
- b) the Society's objects, and the mode and purposes that its funds are to be applied to;
- c) the qualifications and annual membership subscription;
- d) the method of electing new members;
- e) the manner of making, altering and rescinding rules;
- f) the mode of holding meetings and voting;
- g) the appointment and removal of a management committee, or failure to observe any rule, or for misconduct; and
- h) the voluntary dissolution of the organisation (society) and the disposition of the society's property.²⁵⁷

The requirement for associations to have rules that provide for matters outlined in the statute's Schedule remain a condition across all Australian jurisdictions for registration and

²⁵³ Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 15. Limited liability equates to a member's liability is restricted is restricted to the amount of the annual membership fee. Refer to Chapter 4.3.6 of this thesis for a further explanation of members' liability.

²⁵⁴ Except for Western Australia, Australia's other state and territory association legislations have disposed of the requirement to advertise for the purpose of incorporation. Section 6 states that an association must advertise in a newspaper in an area where the association is situated and where it will conduct its affairs. *Associations Incorporation Act 1987* (WA).

²⁵⁵ *Unclassified Societies Registration Act 1895* (NZ) ss13,16–17 in Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 216.

²⁵⁶ *Unclassified Societies Registration Act 1906* (NZ) s 4 in Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 216.

²⁵⁷ *Unclassified Societies Registration Act 1906* (NZ) s 5 in Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 216–217 n 59.

incorporation.²⁵⁸ However, over time, the *Unclassified Societies Acts* of 1895 and 1906 were shown to be inadequate and they were repealed and consolidated into the *Incorporated Societies Act 1908* (NZ).²⁵⁹

The aim of the *Incorporated Societies Act 1908* (NZ) was to improve the preceding Act in relation to incorporation, management, control and the dissolution of societies.²⁶⁰ For the first time in statute, the *Incorporated Societies Act 1908* (NZ) acknowledged that societies can make a profit, but a pecuniary gain was prohibited from being distributed to its members.²⁶¹ The significance of this provision, perhaps unknown at the time, is instrumental in distinguishing between a for-profit and not-for-profit organisation.²⁶² While the preceding Acts were generous towards the range and nature of groups that qualified for incorporation, nevertheless some groups found themselves outside the scope of the Act.²⁶³ The Victoria Students' Hostel complained to the government of the day when they were not granted with incorporation under the *Unclassified Societies Acts 1895-1906* (NZ) on the basis that the hostel was considered to be in receipt of a pecuniary gain by accepting boarding fees.²⁶⁴ The *Incorporated Societies Act 1908* (NZ) resolved

²⁵⁸ *Associations Incorporation Act 1981* (Qld) s 9; *Associations Incorporation Regulation 1999* (Qld) reg 7; *Associations Incorporation Act 2009* (NSW) ss3(c)-(d); *Associations Incorporation Act 1981* (Vic) s5(c)(i); *Associations Incorporation Reform Act 2012* (Vic) s 5(1)(b()); *Associations Incorporation Act 1964* (Tas) s 7(2)(b)(i); *Associations Incorporation Act 1985* (SA) s 19(2)(a); *Associations Incorporation Act 1987* (WA) s5(2)(a); and *Associations Act 2000* (NT) s 8(4).

²⁵⁹ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 216. The original purpose of the *Unclassified Societies Acts 1895–1906* (NZ) had become out-dated as societies were becoming more complex and some legal deficiencies had emerged. The Attorney General of the day did not shed any light on these legal deficiencies. Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 17.

²⁶⁰ Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 18.

²⁶¹ *Incorporated Associations Act 1908* (NZ) s 5 in Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 217 n61. This provision was established long before Hansmann developed the non-distribution theory.

²⁶² This provision has formed the basis for the works of Hansmann's non-distribution theory. See Part 2.2 of this thesis for a further explanation of the non-distribution feature in the structural-operation definition, and Part 2.4 for a discussion of the non-distribution principle.

²⁶³ New Zealand, *Parliamentary Debates*, 1908, 143 N.Z.P.D. 155 (Joseph Ward, Attorney-General) in Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 217 n 62.

²⁶⁴ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 217.

this problem for the hostel, and a wider range of associations and societies then qualified for incorporation.²⁶⁵

Another innovative feature introduced by the *Incorporated Societies Act 1908* (NZ) was the requirement on societies to submit an annual return to the Registrar, and for the organisation's financial statements to be available for public inspection.²⁶⁶ While the annual submission of financial reports today is considered a mechanism of good governance, the intent behind this obligation was not for fiscal accountability, but rather to afford the Registrar with an opportunity to monitor that those organisations were acting within their objectives.²⁶⁷ Perhaps without realising it at the time, the drafter of this Act, Sir John Salmond, had laid the original foundations for the proper administration and management of not-for-profit organisations.

3.5 Sir John Salmond's Model of Incorporation

Sir John Salmond arrived in New Zealand from the University of Adelaide in March of 1906, and in the following year he took the position of Counsel in the Law Drafting Office.²⁶⁸ Salmond's *Incorporated Societies Act 1908* (NZ) is assessed by Fletcher as an 'embellishment' of corporate law.²⁶⁹ This view by Fletcher overlooks Salmond's extensive knowledge of corporate and jurisprudential theory, which can be seen in Sir John Salmond's *Incorporated Societies Act*.²⁷⁰

Salmond's renowned work *Jurisprudence*²⁷¹ distinguishes corporations from a natural person and he describes a legal person as a product of the law's attribution 'by way of fiction'.²⁷² According to Salmond, groups are legally recognised collectives (including corporations and not-

²⁶⁵ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 217.

²⁶⁶ Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 18-44.

²⁶⁷ Douglas White, *The Law Relating to Associations Registered under the Incorporated Societies Act 1903* (LLM Thesis, Victoria University of Wellington, March 1972) 18.

²⁶⁸ Sir John Salmond was Professor of Law at the University of Adelaide from 1897 to 1906. RFV Heuston, 'Sir John Salmond' (1964) 2(2) *Adelaide Law Review* 220, 221; Alex Frame, 'Fictions in the Thought of Sir John Salmond' (1999) 30(1) *Victoria University of Wellington Law Review* 32, [1] <<http://www.austlii.edu.au/journals/VUWLRev/199/32.html>>. Sir Salmond held the position of Counsel from 1907 to 1910. Alex Frame, *Salmond Southern Jurist* (Victoria University Press, 1995) 88.

²⁶⁹ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 221.

²⁷⁰ Alex Frame, *Salmond Southern Jurist* (Victoria University Press, 1995) 288.

²⁷¹ John Salmond, *Jurisprudence* (Sweet & Maxwell, 2nd ed, 1893) 68.

²⁷² Alex Frame, *Salmond Southern Jurist* (Victoria University Press, 1995) 68; John Salmond, *Jurisprudence or The Theory of The Law* (Stevens & Haynes, 1902) 344-345.

for-profit organisations) as having a legal personality provided by the law and the state.²⁷³ This juristic personality of corporations as seen by Salmond is fictitious and he acknowledged that ‘a group of people is a very real thing, but it is only a fictitious person’.²⁷⁴ Although Salmond developed his fiction theory before taking the role as Counsel, his fiction theory can be located in his Act.²⁷⁵

Salmond was also of the opinion that the role of the State was to encourage and empower groups, regardless of whether the group’s legal personality is real or fiction.²⁷⁶ Furthermore, Salmond saw that through the attribution of law, members of a company should have interests, rights, and be protected from liability.²⁷⁷ Reflecting this view, Salmond’s *Incorporated Societies Act 1908* (NZ) created the legal requirement for incorporated societies to have objects and rules that gave a society’s members’ rights and limited liability – moreover, his Act separated a society’s obligations from its members.²⁷⁸ Salmond’s *Incorporation Societies Act 1909* (NZ) has had a wide-reaching influence across the Tasman to Australia.

When it came time for Queensland, Western Australia and New South Wales to enact their own incorporated associations’ legislation, these states closely followed New Zealand’s Act²⁷⁹ and largely ignored the South Australian model.²⁸⁰ Although South Australia is credited for the creation of the incorporated association it is, however, New Zealand’s, and particularly Salmond’s model, which has shaped and had a lasting influence on the incorporated association model adopted by these states. Nevertheless, in more recent times Salmond’s model has been subject to scrutiny as concerns are raised about its suitability in meeting today’s needs for

²⁷³ John Salmond, *Jurisprudence or The Theory of The Law* (Stevens & Haynes, 1902) 344-345; Alex Frame, *Salmond Southern Jurist* (Victoria University Press, 1995) 68.

²⁷⁴ Alex Frame, *Salmond Southern Jurist* (Victoria University Press, 1995) 71; John Salmond, *Jurisprudence or The Theory of The Law* (Stevens & Haynes, 1902) 364.

²⁷⁵ Alex Frame, *Salmond Southern Jurist* (Victoria University Press, 1995) 68.

²⁷⁶ Alex Frame, ‘Fictions in the Thought of Sir John Salmond’ (1999) 30(1) *Victoria University of Wellington Law Review* 32, [32]-[33] <<http://www.austlii.edu.au/journals/VUWLRev/199/32.html>>.

²⁷⁷ John Salmond, *Jurisprudence* (Sweet & Maxwell, 2nd ed, 1893) in John Farrar, ‘Salmond and Corporate Theory’ (2007) 38 *Victoria University of Wellington Law Review* 925, 928.

²⁷⁸ John Farrar, ‘Salmond and Corporate Theory’ (2007) 38 *Victoria University of Wellington Law Review* 925, 930.

²⁷⁹ The features that these states took from the *Incorporated Societies Act 1909* (NZ) were: the simplified incorporation process; the provision of a minimum content for association rules; the submission of an annual financial return; and outline procedures for the dissolution and cancellation of incorporation. Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 221.

²⁸⁰ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 221.

transparent administration.²⁸¹ Addressing these concerns, New Zealand's Law Commission is undertaking a comprehensive review of their incorporated association structure to see how this organisational form can be improved to satisfy the need for transparency.²⁸²

3.6 Conclusion

The concept of a cheap and simple organisational form for non-profit associations was needed to overcome the ills of charitable trusts. South Australia's parliament developed an organisational form that would permit not-for-profit institutions to self-manage their property (without it being vested in a trustee). However, despite some limitations in the earlier South Australian model, the incorporated association legislation was amended a number of times, and this reflected some aspects of the New Zealand model of incorporation.

New Zealand's earlier model of incorporation was less restrictive and more advanced than South Australia's model as it offered a simple process of incorporation. It provided members with limited liability, introduced a central registry, established the requirement for an association to file a set of rules when applying for incorporation, and required the submission of an annual report for public inspection. These requirements were subsequently introduced into the South Australian model and remain in force today across all Australian jurisdictions. Perhaps the most significant features of New Zealand's statute is that it acknowledged societies could make a profit, and that they are prohibited from distributing profit to their members. The drafter of this innovative incorporated model was Sir John Salmond; his in-depth understanding of jurisprudential and corporate theory greatly attributed to the development of the model of incorporation.

²⁸¹ New Zealand Law Commission, *Review of the Incorporated Societies Act 1908* (4 August 2011) <<http://www.lawcom.govt.nz/project/review-incorporated-societies-act-1908>>.

²⁸² It is not within the scope of this thesis to examine and analyse the Law Commission's report and recommendations.

CHAPTER 4: Legal Forms for Organising Not-for-Profit Organisations

*Clubs engage in activities which are designed to raise money such as [sic] poker machines, liquor sales, bingo games and the like. There may ... come a time when these other activities take a life on their own, they become an end in themselves.*²⁸³

4.0 Introduction

The law, unlike economic and social theories, is not concerned about the space in which not-for-profit organisations operate, but rather the form of the not-for-profit.²⁸⁴ Compared to the private and public sectors, the not-for-profit sector encompasses a larger number of unique entities: associations; unincorporated associations; incorporated associations; trading associations; charitable trusts; companies limited by guarantee; cooperative societies; and friendly societies – each form has subtly different characteristics. This chapter provides a basic understanding of the four main entities in the sector: associations; unincorporated and incorporated associations; and companies limited by guarantee. To appreciate and understand these entities, each entity’s characteristics are briefly outlined.

4.1 Associations

4.1.1 Definition

Often the term ‘association’ in the not-for-profit sector is prefixed with ‘unincorporated’ or ‘incorporated’. The term ‘association’ describes a combination of people who possess a common interest or purpose with a degree of organisation and, moreover, continuity.²⁸⁵ Having a degree of organisation and continuity is sufficient to distinguish an association from an *ad hoc* group of

²⁸³ *St Mary’s Rugby League Club Ltd v The Commissioner for Taxation* (1997) 97 ATC 4528 at 4529–4530.

²⁸⁴ Kim Weinert, ‘Is a Small Revolution Really too Much to Ask For?’ (Paper presented at the Sydney Law School Postgraduate Conference, Law and Social Reality, 29 October 2010) 2.

²⁸⁵ *Smith v Anderson* (1880) 15 Ch D 247, 273.

individuals. Further, an association will also have some criteria or clear method for identifying its members.²⁸⁶

Queensland's legislation defines an association to mean an association, society, body or another entity formed and/or to carry on a lawful purpose.²⁸⁷ This provision, and the other respective provisions across jurisdictions, do not offer a helpful description of an association. An association is best described to be, in a broad sense, a group of individuals (usually two or more people) who have agreed (voluntarily) to join together in pursuit of one or more common purpose/s.²⁸⁸ Not-for-profit associations will promote, *inter alia*, religious, educational, literary, scientific, artistic, and other benevolent purposes that will benefit the general community, as well as members of the association.²⁸⁹

4.2 Unincorporated Associations

4.2.1 Definition

Unincorporated associations are formed when groups of people come together who share a common lawful purpose, and agree to further that interest by collective action. However, for legal purposes, an unincorporated association is considered to be an aggregate of its members at a particular time.²⁹⁰ There are three essential characteristics of an unincorporated association:

- 1) the association has members who are free to join or resign at will;²⁹¹
- 2) there must be a contract between the members and the association, *inter se*;²⁹² and
- 3) there must be 'a matter of history'.²⁹³

²⁸⁶ *Kibby v Registrar of Title* [1999] 1 VR 861.

²⁸⁷ *Associations Incorporated Act 1981* (Qld) s 2. Also see, *Associations Act 2003* (NT) s 4; *Associations Incorporation Act 1985* (SA) s 18(1); *Associations Incorporation Act 1964* (Tas) s 2(1); *Associations Incorporation Act* (Vic) s 3(1); *Associations Incorporation Reform Act 2012* (Vic) s 3; *Associations Incorporation Act 1987* (WA) s 3(1); *Associations Incorporation Act 2009* s 4(1). The term association is not defined in the *Associations Incorporation Act 1991* (ACT).

²⁸⁸ *Smith v Anderson* (1880) 15 Ch D 247.

²⁸⁹ LexisNexis, *Halsbury's Laws of Australia*, vol 28 (at 3 April 2012) 316 Voluntary Associations, '(b) Definition and Classification of Not-for-Profit Associations' [435–10].

²⁹⁰ *Wilson v J & AG Johnson Ltd* (1939) 55 CLR 63, 67.

²⁹¹ *Conservative and Unionist central Office v Burrell* [1980] 3 All ER 42.

²⁹² *John v Rees* [1970] Ch 345 affirmed that there is a contractual effect to relationship between members and the unincorporated association.

²⁹³ The phrase 'a matter of history' refers to a moment in time when a number of persons came together to form the association. *Conservative and Unionist Central Office v Burrell* [1980] 3 All ER 42, 58.

An unincorporated association is formed by the voluntary action of those people who agree to its formation and the association's terms.²⁹⁴ Furthermore, individuals must not gain a direct pecuniary advantage from the association.²⁹⁵

4.2.2 *Membership Entry and Rights*

The original members of an unincorporated association must decide on how to regulate the admission, suspension, or expulsion of members.²⁹⁶ Such decisions and conventions are agreed by the association's original members and should be stated in the association's rules.²⁹⁷ The unincorporated association can receive a membership fee when an individual becomes a member. Membership will continue indefinitely provided the membership fee or subscription fee is paid as required by the rules of the association.²⁹⁸ A member of an unincorporated association enjoys the use of the association's property and participation in the association's activities providing the association remains in existence.²⁹⁹

4.2.3 *Legal Standing*

An unincorporated association has no separate legal personality from its members and is not recognised in law regardless that 'to the man on the street' and to its members the association is real.³⁰⁰ This lack of legal status causes many difficulties for members in areas that are addressed later in this section.³⁰¹ Furthermore, due to the lack of perpetual succession with unincorporated associations, the acquiring and disposing of property has shown to be a problematic area. With no legal standing, property must be vested in the names of individual members or in trustees rather than in the association's name.³⁰²

²⁹⁴ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 2nd ed, 1996) 2.

²⁹⁵ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 11.

²⁹⁶ An association may adopt an admission policy where membership to an association is necessary for an individual to carry on a trade or profession, or where the respective anti-discrimination legislation applies. However, Queensland's *Anti-Discrimination Act 1991* excludes not-for-profit associations.

²⁹⁷ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 12.

²⁹⁸ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 3.

²⁹⁹ *Re St James' Club* (1852) 42 ER 920.

³⁰⁰ *Worthing Rugby Football Club Trustees v Inland Revenue Commissioners* [1985] 1 WLR 409, 413 (Gibson J).

³⁰¹ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 6.

³⁰² A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 7.

4.2.4 Liability

Not being a separate legal entity, an unincorporated association denotes that *all* members will be jointly liable and will equally share the loss or damage sustained by the unincorporated association.³⁰³ However, committee members may be indemnified from the unincorporated association's funds for any liability incurred in performing their duties.³⁰⁴ Should an unincorporated association not hold the adequate funds to meet the liability, then the individual members are personally liable.³⁰⁵

4.2.5 Sources of Revenue and Gifts

The viability of an unincorporated association is largely achieved by two methods: through membership subscriptions and fees; or through some revenue from public commercial activities, such as entertainment or games of chance.³⁰⁶ Members of the unincorporated association, as well as members of the public, may provide gifts to the association by donations or by will.³⁰⁷

Receiving testamentary gifts is problematic for unincorporated associations owing to the lack of legal personality. An unincorporated association cannot validly accept a gift by will, as this may be a breach of the Rule Against Perpetuities.³⁰⁸ However, the courts are willing to give effect to a gift (by *inter vivos* or by will) where an unincorporated association's objects are charitable.³⁰⁹

4.2.6 Rules

The rules of an association regulate matters such as the purpose of the association, admission and expulsion of members, management of the association's affairs, and property.³¹⁰ It is not essential that an unincorporated association has a written constitution or rules;³¹¹ however, the rules of

³⁰³ *Miller v Jackson* [1977] QB 966; *Bradley Egg Farm Ltd v Clifford* [1943] 2 All ER 378.

³⁰⁴ *Peckham v Moore* [1975] 1 NSWLR 353.

³⁰⁵ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 39.

³⁰⁶ An amount prescribed under the association's rules and constitution.

³⁰⁷ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 23.

³⁰⁸ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 22.

³⁰⁹ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 23–24.

³¹⁰ *Conservative and Unionist Central Office v Burrell* [1980] 2 All ER 42.

³¹¹ *Kibby v Registrar of Titles* [1999] 1 VR 861.

unincorporated associations are sometimes found to be inadequate;³¹² for example, failing to provide procedures on how to dissolve the association and dispose of property.³¹³

The rules or constitution of an unincorporated association are a private arrangement between members, but is this agreement a legally enforceable contract? Traditionally, under the decision of *Cameron v Hogan*, this private arrangement is held not to be a contractual relationship, but a consensual one.³¹⁴ Therefore, any written rules of the association are for governing the association and are not an enforceable contract.³¹⁵ However, the courts may find the rules of an unincorporated association (and incorporated association) to be legally binding where a member's right of a proprietary nature can be enforced, and/or there is an injury to a member's economic interest, such as a restraint of trade.³¹⁶

4.2.7 *Management Committee and Power*

The rules of an unincorporated association should provide for the management of the association's activities by a committee; however, the members are free to decide on a management structure.³¹⁷ The association's rules should detail the management committee's power and duties and allow for the members to challenge decisions that are made outside the scope of the association's objective/s.³¹⁸

³¹² *Ball v Pearsall* (1987) 10 NSWLR 700.

³¹³ See *Re Producers' Defence Fund* [1954] VR 246; *Abbatt v Treasury Solicitor* [1969] 3 All ER 1175; *Master Grocers' Association of Victoria v Northern District Grocers Co-Operative Ltd* [1983] VR 195.

³¹⁴ *Cameron v Hogan* (1934) 51 CLR 358.

³¹⁵ *Cameron v Hogan* (1934) 51 CLR 358. See also *Plenty v Seventh Day Adventist Church of Port Pirie* (1986) 40 SASR 443.

³¹⁶ *Cameron v Hogan* (1934) 51 CLR 358, 370 (Rich, Dixon, Evatt and McTiernan JJ); *Hawick v Flegg* (1958) 74 WN (NSW) 255.

³¹⁷ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 17.

³¹⁸ *Stevens v Keogh* (1946) 72 CLR 1; *Clark v University of Melbourne* [1978] VR 457.

4.3 Incorporated Associations

4.3.1 Definition

An incorporated association is one incorporated under either the respective associations incorporation act,³¹⁹ by royal charter, or a special act of parliament.³²⁰ The type of association eligible for incorporation must:³²¹

- be formed for a legal purpose or objective;
- have at least a certain number of members (as prescribed under the respective state and territory legislation);³²² and
- not be for providing financial gain for its members.³²³

An incorporated association has the powers of an individual to: enter into contracts; acquire, hold, deal with and dispose of property; charge for services and facilities that it may supply; do

³¹⁹ *Associations Incorporation Act 1981* (Qld) s2; *Associations Incorporation Act 1991* (ACT) s 14; *Associations Incorporation Act 2009* (NSW) s 6; *Associations Incorporation Act 1981* (Vic) s 3; *Associations Incorporation Reform Act 2012* (Vic) s 1(a); *Associations Act 2003* (NT) s 8; *Associations Incorporation Act 1987* (WA) s 4; *Associations Incorporation Act 1964* (Tas) s 8; *Association Incorporation Act 1985* (SA) s20.

³²⁰ Moreover, incorporation is a process of formal recognition by issuing a certificate of incorporation and a seal. State government departments determine the process of incorporation, and their main role is to ensure those applying for incorporation meets the legislative criteria and payment of fees.

³²¹ Not all associations can be incorporated under the *Associations Incorporation Act 1981* (Qld). For example, section 5 of the Act prohibits: a society registered under the *Friendly Societies Act 1991* (Qld); an industrial organisation under the *Industrial Relations Act 1999* (Qld); school councils or Parents' and Citizens' Associations created under the *Education (General Provisions) Act 1989* (Qld); bodies that raise monies by subscription and lends that monies to its members; an association by a special Act of Parliament; and an association that holds property that its members may divide amongst themselves, dispose of their interest, or distribute income or the use of the property amongst its members or member's nominees.

³²² *Associations Incorporation Act 1981* (Qld) s 5(1)(a) requires not less than seven members; *Associations Incorporation 1991* (ACT) s 15(a) and *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 7 requires at least five members; *Associations Incorporation Act 2009* (NSW) s 6(1)(b) requires five or more members; *Associations Incorporation Act 1987* (WA) s 5(2)(b)(v) requires at least five members; *Associations Act 2003* (NT) s 26 requires not less than five members. There are no provisions contained in the respective associations' legislation in the jurisdictions of Tasmania and South Australia.

³²³ *Associations Incorporation Act 1981* (Qld) s 5. The term 'financial gain' is defined by section 4 of the *Associations Incorporation Act 1981* (Qld) to be a gain from trade, charging admission fees to displays, exhibitions, contests, sporting fixtures, or other events that promotes its objects, or subscription fees or receiving donations. The term 'financial gain' is also interchangeable with the term 'pecuniary gain'. See *Associations Incorporation Act 1991* (ACT) s 4; *Associations Incorporation Act 2009* (NSW) s 5(1); *Associations Incorporation Act 1987* (WA) s 4(4); *Associations Incorporation Act 1985* (SA) s 5(a)-(6)(a); *Associations Incorporation Act 1964* (Tas) s 21(2); *Associations Incorporation Refrom Act 2012* (Vic) s 33(1)-(3). Under the Northern Territory statute, section 13A(2) prohibits an incorporated association from distribute profits to its members; however, this specific provision does not apply to a trading association (which is incorporated under the *Associations Act 2003* (NT)).

other things necessary to be done in carrying out its affairs; and may issue secured and unsecured notes, debenture stock for the association.³²⁴

4.3.2 *Legal Status*

Incorporating an association creates an artificial legal person that is a body corporate.³²⁵ An incorporated association becomes, at law, a legal body with a personality, rights and liabilities separate from the association's members.³²⁶ An incorporated association has superior legal status over an unincorporated association, which has no legal status. An incorporated association is a legal entity and, in its own name, has the capacity to sue and to be sued.³²⁷

4.3.3 *Membership Entry and Rights*

The rules or constitution of an incorporated association clearly set out: qualifications needed for membership; subscription fees; and a member's rights, privileges and duties.³²⁸ Akin to an unincorporated association, a member of an incorporated association will not be considered a member until payment of a subscription or entrance fee is made pursuant to the association's rules.³²⁹ Should a considerable time have lapsed and a person has failed to pay their membership fee, then that person is not to be considered a member.³³⁰ Once a membership fee or subscription

³²⁴ *Associations Incorporation Act 1981* (Qld) ss 21, 25; *Associations Incorporation Act 1991* (ACT) s 22; *Associations Act 2003* (NT) s 11; *Associations Incorporation Act 2009* (NSW) ss 8, 9, 19; *Associations Incorporation Act 1985* (SA) s 20; *Associations Incorporation Act 1964* (Tas) s 11; *Associations Incorporation Act 1981* (Vic) s 14; *Associations Incorporation Reform Act 2012* (Vic) pt 4, dv, s 29; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 5

³²⁵ Upon incorporation, the entity will have perpetual succession and a common seal. A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed., 2010) 122.

³²⁶ A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 122–124.

³²⁷ LexisNexis, *Halsbury's Laws of Australia*, vol 28 (at 3 April 2012) 316 Voluntary Associations, '(a) A Name – Effect of Incorporation' [435–85].

³²⁸ *Associations Incorporation Regulation 1999* (Qld) reg 7, sch 3 pt 1 regs 3–5; *Associations Incorporation Act 1991* (ACT) sch 1; *Associations Incorporation Act 2009* (NSW) sch 1; *Associations Act 2003* (NT) dv 4 s 21; *Associations Incorporated Act 1981* (Vic) s 21; *Associations Incorporation Reform Act 2012* (Vic) ss 48, 49, sch 1; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, pt 3; *Incorporated Associations Act 1985* (SA) 23A; *Associations Incorporation Act 1987* (WA) sch 1; *Associations Incorporation Act 1964* (Tas) s 16.

³²⁹ *Re New University Club (Duty on Estate)* (1887) 18 QBD 720 at 727. See also *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 12.

³³⁰ *Re Sick and Funeral Society of St John's Sunday School, Golcar* [1973] Ch 51.

has been paid, the ratification of membership occurs at a general meeting, or at a special meeting under the association's rules.³³¹

Members may resign from an incorporated association at their will.³³² Generally, the association's rules will set out the procedure on how members are to resign.³³³ Should the rules not provide for this procedure then, similar to resigning from an unincorporated association, a member must notify the association's secretary of an intention to resign, either orally or in writing.³³⁴ Resignation will take effect immediately without the need of the committee's acceptance or a general meeting.³³⁵

4.3.4 Rules

An association's rules constitute the terms of the contract between its members and the association.³³⁶ This section also provides members with the statutory right to apply to the Supreme Court for a judicial review of an association's decision when a member is deprived of a right³³⁷ conferred by the association's rules.³³⁸ An incorporated association is bound to the rules of natural justice when dealing with such matters.³³⁹

³³¹ *Associations Incorporation Regulation 1999* (Qld) regs 8–9, sch 4; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 11.

³³² LexisNexis, *Halsbury's Laws of Australia*, vol 28 (at 3 April 2012) 316 Voluntary Associations, '(h) Admission to Membership' [435-155].

³³³ A.S. Seivers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 1996) 59.

³³⁴ *Finch v Oake* [1896] 1 Ch 409.

³³⁵ *Finch v Oake* [1896] 1 Ch 409.

³³⁶ *Verduci v Catanzarita* (1981) 53 FLR 156; *Islamic Council of South Australia Inc v Australian Federation of Islamic Councils Inc* [2009] NSWSC 211; *Rose v Boxing NSW Inc* [2007] NSWSC 20. See also *Associations Incorporation Reform Act 2012* (Vic) s 46.

³³⁷ A member's right under the rules are voting, being eligible to or holding office. *Associations Incorporation Regulation 1999* (Qld) sch 3, pt 2(2).

³³⁸ The Supreme Court has the power to make orders to have an association's rules observed, declaring or enforcing member's rights (despite the members having no interest in property), grant relief, or refuse an application and order costs. *Associations Incorporation Act 1981* (Qld) ss 72, 73; *Associations Incorporation 1985* (SA) 24(1). Within Victoria matters that are to go before the Supreme Court are: a complex question; a matter of general importance; or a question of law only determinative by the Supreme Court. Therefore all other proceedings are before the Magistrates' Court. *Associations Incorporation Reform Act 2012* (Vic) s 220.

³³⁹ *Associations Incorporation Act 1981* (Qld) s 71(3); *Associations Incorporation Act 1991* (ACT) s 50; *Associations Incorporation Act 1985* (SA) s 40; *Associations Incorporation Act 1981* (Vic) s 14B(3); *Associations Act 2003* (NT) s 39, sch 1; *Associations Incorporation Regulation 2010* (NSW) Sch 1; *Associations Incorporation Regulations 2008* (SA) sch 1; *Associations Incorporation Regulations 2009* (Vic) sch 4; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, dv 2 provides a clear procedure and time-frames for the association to undertake when the need arises to for an association to undertake disciplinary action against a member. Furthermore, this specific procedure reflects the principles of natural justice. *Associations Regulations* (NT) Sch 1; *Associations Incorporation Regulations 1999* (Qld) Pt 3 dv 1. See also *McClelland v Burning Palms Surf Life Saving Club* [2002] NSWSC 470.

Model rules for an incorporated association are annexed to the legislation and can usually be found in its regulations.³⁴⁰ These model rules have been drafted to provide a structure for an association to manage its affairs, appoint a committee, decide membership rights and entry requirement, and decide when to meet legislative requirements, such as financial reporting.³⁴¹ The model rules are to be adopted by the association, or altered to suite its needs.³⁴²

4.3.5 Source of Revenue

Like any other entity, an incorporated association must remain viable to meet its purpose and to deliver its services. Similar to unincorporated associations, many incorporated ones rely on the same sources of revenue, as well as membership subscriptions and fees.³⁴³ However, unlike an unincorporated association, an incorporated one is subject to a minimal standard of financial accountability.³⁴⁴

This financial accountability leads to incorporated associations qualifying for government grants. Furthermore, being an incorporated association sees the willingness of governments to provide financial support over and above an unincorporated association. Many associations give the impression they are a highly commercial entity and that they trade for the benefit for the

³⁴⁰ *Associations Incorporation Act 1981* (Qld) s 60 and see sch 4 in the *Associations Incorporation Regulations 1999* (Qld) for a copy of these model rules.

³⁴¹ *Associations Incorporation Act 1981* (Qld) s 48; *Associations Incorporation Act 2009* (NSW) s 23; *Associations Incorporation Act 1981* (Vic) s 22; *Associations Incorporation Reform Act 2012* (Vic) ss 103, 104; *Associations Incorporation 1964* (Tas) s 18; *Associations Incorporation Act 1991* (ACT) ss 30, 33; *Associations Act 2003* (NT) s 23. See also *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, pt 5, dv 1.

³⁴² When associations decide to amend their rules, it must be done by special resolution and, within three (3) months of the special resolution, the associations must apply to the respective state department for approval. The chief executive may either grant or refuse the application for an association to amend the model rules. *Associations Incorporation Act 1981* (Qld) ss 48(2A), (5); *Associations Incorporation Act 1964* (Tas) s 18(4); *Associations Incorporation Act 1987* (WA) s 19. In the Northern Territory and Victoria, any amendments to an association's rules are to be passed by its members by a special resolution. *Associations Act 2003* (NT) s 21(1)(g); *Associations Incorporation Reform Act 2012* (Vic) s 49(4)(b). For Victorian, New South Wales and South Australian associations their amended rules will take effect when the Commissioner or the Director-General approves the new rules. *Associations Incorporation Act 1981* (Vic) s 22(4); *Associations Incorporation Reform Act 2012* (Vic) s 50(2); *Associations Incorporation Act 2009* (NSW) ss 12, 14; *Associations Incorporation Act 1985* (SA) s 24(2).

³⁴³ Members from time to time at an Annual General Meeting will determine an amount prescribed under the association's rules or constitution. *Associations Incorporation Regulations 1999* (Qld) sch 4, s 8.

³⁴⁴ *Associations Incorporation Regulations 1999* (Qld) regs 9-12, 46, sch 4; *Associations Incorporation Act 2009* (NSW) ss 42, 46, 50(1); *Associations Incorporation Act 1987* (WA) ss 25, 26; *Associations Incorporation Act 1985* (SA) ss 35; *Associations Incorporation Regulations 2008* (SA) r 4; *Associations Incorporation Act 1981* (Vic) ss 41, 32, 43, 47; *Associations Incorporation Reform Act 2012* (Vic) pt 7; *Associations Incorporation Regulations 2010* (Vic) regs 10, 11, Sch 4; *Associations Incorporation Act 1991* (ACT) ss 71, 72, 73, 74, 79; *Associations Incorporation Regulations 1991* (ACT) regs 12-13; *Associations Incorporation Act 1964* (Tas) ss 24, 24B. Some jurisdictions have created tiered financial reporting obligations. Appendix 1 outlines the tiered financial reporting obligations and thresholds for associations.

association's business rather than its members. If a profit has been made incidental to the association's activities, the profit must be applied exclusively to achieving the association's objects and the lawful purpose of the association.³⁴⁵

4.3.6 Liability

Members of an incorporated association have limited liability, which equates to a member's liability being restricted to the amount of the annual membership fee.³⁴⁶ Limited liability also extends to committee members and other members.³⁴⁷

The application of limited liability is two-fold. First, members are not liable to contribute payment towards the association's debts if it is wound up or insolvent. Secondly, if the association has been unsuccessful in litigation, then members are only liable to the amount that they have paid in subscription or membership fees.³⁴⁸ Furthermore, a member of an incorporated association may be afforded statutory protection.³⁴⁹

The *Civil Liability Act 2003* (Qld) (the CLA) states that a volunteer undertaking community work is protected from any civil liability.³⁵⁰ It goes on to state that the association or an office-holder of the association must coordinate this work in good faith.³⁵¹ The CLA does not offer protection where a volunteer has acted outside the association's instructions or not in good faith – therefore, it is likely that a court would find the individual personally liable.³⁵²

³⁴⁵ Geoffrey Egert, 'Legal Capacity of Incorporated Associations and the Associations Incorporation Act 1981 (Qld)' (2001) 8 *James Cook University Law Review* 41.

³⁴⁶ A. S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 123.

³⁴⁷ A. S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 123.

³⁴⁸ *Wise v Perpetual Trustee Co Ltd* [1903] AC 139.

³⁴⁹ Volunteer immunity provisions are also found in other state and territory legislation similar to the CLA. However, this thesis only analyses the CLA. See *Civil Liability (Wrongs) Act 2002* (ACT) s 8; *Civil Liability Act 2002* (NSW) s 61; *Personal Injuries (Liability and Damages) Act 2002* (NT) s 7(1); *Volunteers Protection Act 2001* (SA) s 4; *Civil Liability Act 2002* (Tas) s 47; *Wrongs Act 1958* (Vic) s 37; *Volunteers (Protection from Liability) Act 2002* (WA) s 6(1). Furthermore, the association legislation in Victoria, Western Australia, New South Wales and the Northern Territory provides committee members with protection from civil liability. *Associations Incorporation Reform Act 2012* (Vic) s 87; *Associations Incorporation Act 1987* (WA) s 39D; *Associations Incorporation Act 2009* (NSW) s 103; *Associations Act 2003* (NT) s 82(2).

³⁵⁰ The CLA does not specify what is meant by 'any civil liability' and, therefore, this phrase may refer to any actions in torts and contracts brought against the association. Barbara McDonald, 'Indemnities and the Civil Liability Legislation' (2011) 27(1–2) *Journal of Contract Law* 58. Furthermore, 'community work' is to mean work done for a charitable, benevolent, philanthropic, sporting, political, educational, recreational or cultural purposes, and is not done for private financial gain. *Civil Liability Act 2003* (Qld) s 38(c).

³⁵¹ *Civil Liability Act 2003* (Qld) s 39.

³⁵² *Civil Liability Act 2003* (Qld) s 42.

However, there are further restrictions to a volunteer's immunity under the CLA. Volunteers will only benefit from the CLA if their community work is undertaken within a community organisation as defined by the CLA:³⁵³ a corporation; a trustee (or acting in the capacity of trustee); a political party;³⁵⁴ a public authority;³⁵⁵ a parent and citizens' association;³⁵⁶ or any entity prescribed under its regulation.³⁵⁷ The entities prescribed in Schedule 2 of the *Civil Liability Regulation 2003* (Qld) are those that perform duties and services to enhance public safety to a person in distress (that is rendering first aid, other aid, or assistance).³⁵⁸ The application of these provisions excludes a sizable proportion of the not-for-sector, and volunteers that carry on activities outside the prescribed ones in the CLA and its regulations. The construction of these provisions offers little incentive to individuals and to organisations to undertake community work.³⁵⁹

4.3.7 Management Committee

The model rules of an incorporated association provide for the composition of the association's management committee. Figure 3 illustrates a general and common structure of a management committee found within an incorporated association.³⁶⁰

All officer holders of the management committee are appointed or elected to their respective positions. How individuals are elected is provided by the rules of the association.³⁶¹ Once an individual has been elected, there are legislative requirements for a management committee

³⁵³ *Civil Liability Act 2003* (Qld) s 26.

³⁵⁴ A political party must be registered and defined under the *Electoral Act 1992* (Cth) or the *Commonwealth Electoral Act 1918* (Cth). *Civil Liability Act 2003* (Qld) s 38(1)(d).

³⁵⁵ A public or other authority means the Crown, a local government, or any public authority constituted under section 24 of the *Civil Liability Act 2003* (Qld).

³⁵⁶ A parent and citizens' association must be formed under the *Education (General Provisions) Act 2006* (Qld); *Civil Liability Act 2003* (Qld) s 38(1)(f).

³⁵⁷ *Civil Liability Act 2003* (Qld) ss 38(1)(a)–(g).

³⁵⁸ *Civil Liability Act 2003* (Qld) s 27. A person in distress includes one who is injured or at risk of injury, and a one who is suffering, or apparently suffering, from an illness: Section 25 *Civil Liability Act 2003* (Qld). See schedule 2 of *Civil Liability Regulation 2003* (Qld) for a list of prescribed entities that are afforded liability protection. Some entities listed are: Brisbane City Council; Queensland Ambulance Service; and Royal Lifesaving Queensland Incorporated.

³⁵⁹ Norman Katter, 'Civil Liability Reform and the Not-for-Profit Sector Australia' (2005) 11(2) *Third Sector Review* 137 <<http://eprints.qut.edu.au/5212/2/5212.pdf>>.

³⁶⁰ The Model Rules details the composition of a management committee for a Victorian incorporated association. See *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, dv 2.

³⁶¹ *Styles v Ku-ring-gai Historical Society* [2003] NSWSC 926.

structure to be in place to control the association's business and operation.³⁶² However, a person can be excluded from being elected or be required to vacate any position/s on the management committee if that person has been convicted of certain offenses.³⁶³

The management committee of an incorporated association must have the position of a public officer. A public officer is a natural person³⁶⁴ who must reside in the jurisdiction the association is incorporated, and the public officer must fulfil its duties on behalf of the association.³⁶⁵ These duties are primarily to ensure that the incorporated association meets its legislative responsibilities and, to a lesser extent, be a point of contact between the association and the respective government department.³⁶⁶

³⁶² *Re Vassallo* [2001] 1 Qd R 91.

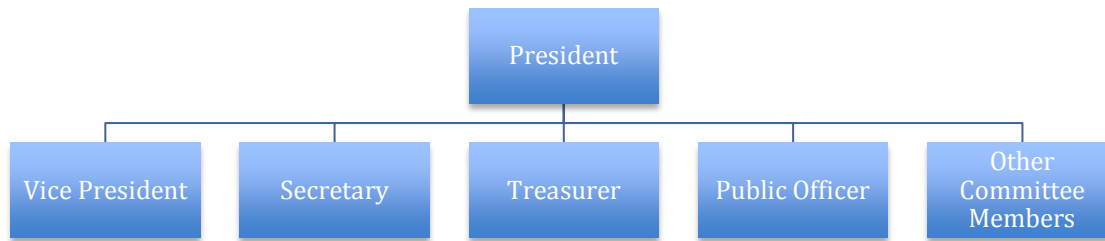
³⁶³ *Associations Incorporation Act 1981* (Qld) s 61A; *Associations Act 2003* (NT) ss 30, 40; *Associations Incorporation Act 2009* (NSW) s 35; *Associations Incorporation Act 1991* (ACT) s 63; *Associations Incorporation Act 1985* (SA) s 30; *Associations Incorporation Act 1981* (Vic) s 27; *Associations Incorporation Reform Act 2012* (Vic) s 78(2)(c); *Associations Incorporation Act 1964* (Tas) s 14(5). Reasons for being excluded from holding a position on a management committee are different in each jurisdiction. Appendix 2 provides an overview of these exclusions in each jurisdiction.

³⁶⁴ *Associations Incorporation Act 1981* (Qld) ss 8, 65, 66(1), 69A; *Associations Incorporation Act 1991* (ACT) ss 57, 58, 59; *Associations Act 2003* (NT) ss 27, 28; *Associations Incorporation Act 2009* (NSW) s 34; *Associations Incorporation Act 1985* (SA) s 56; *Associations Incorporation Act* (Tas) ss 14, 15.. In Queensland, New South Wales, South Australia and Tasmania, a public officer must be over the age of 18. Under the respective provisions of the Northern Territory, New South Wales and Tasmania, a public officer must be a resident within those jurisdictions. However, in Queensland, a public officer is also the association's secretary and must reside within 65 kilometres of the Queensland border. *Associations Incorporation Act 1981* (Qld) s 69(2)(e). The *Associations Incorporation Reform Act 2012* (Vic) has removed the requirement for an association to have a public officer. However, if an association is operating under the old rules then a public officer is now the secretary of the association. *Associations Incorporation Reform Act 2012* (Vic) sch 4, cl 9.

³⁶⁵ LexisNexis, *Halsbury's Laws of Australia*, vol 28 (at 3 April 2012) 316 Voluntary Associations, '(a) Structure – Public Officer' [435-175].

³⁶⁶ The public officer of an incorporated association is responsible to ensure that the association complies with its responsibilities under the legislation, such as lodging financial returns and transferring the association's property. *Associations Incorporated Act 1981* (Qld) ss 21, 24, 52, 59 (4), 70 (2); *Associations Incorporation Act 2009* (NSW) ss 21, 45, 49; *Associations Act 2003* (NT) ss 22(1), 23(4), 54(7); *Associations Incorporation Act 1985* (SA) s 24(3)(b); *Associations Incorporation Act* (Tas) ss 10, 13, 15, 18, 23; *Associations Incorporation Act 1981* (Vic) ss 8, 9, 13, 22, 30; *Associations Incorporation Regulations 2009* (Vic) pt 2; *Associations Incorporation Reform Regulations 2012* (Vic) reg 47.

Figure 3 – Composition of a management committee



4.4 Company Limited by Guarantee

4.4.1 Definition

Associations may become registered as a company limited by guarantee under the *Corporations Act*.³⁶⁷ A company limited by guarantee is defined as a company that is formed on the principle of having members whose liabilities are restricted to the respective amount that the members undertake (or guarantee) to contribute to the property of the company in the event it is wound up.³⁶⁸ Moreover, this type of entity does not have the capacity or the power to issue shares.³⁶⁹

A company limited by guarantee that pursues charitable purposes can omit 'Limited' from its name.³⁷⁰ The *Corporations Act 2001* (Cth) provides that a company limited by guarantee must apply its income to promoting its charitable objects,³⁷¹ and prohibits distribution of this income to its members.³⁷²

³⁶⁷ 2001(Cth).

³⁶⁸ *Corporations Act 2001* (Cth) s 9.

³⁶⁹ *Corporations Act 2001* (Cth) s 124.

³⁷⁰ The admission of the word 'Limited' is by permission of the Australia Securities and Investments Commission ('ASIC'). *Corporations Act 2001* (Cth) s 150.

³⁷¹ *Corporations Act 2001* (Cth) s 150(1)(a).

³⁷² *Corporations Act 2001* (Cth) s 254SA.

4.4.2 Liability

Similar to a member of an incorporated association, a member's liability in a company limited by guarantee is restricted to the amount of the member's guarantee.³⁷³ This means a member will not pay more than the undertaken amount when the company is being wound up.³⁷⁴ Furthermore, as discussed in Part 4.3.6, a corporation is an entity covered by the CLA and, therefore, a member of a company limited by guarantee is afforded the protection of the CLA. However, a company director is not afforded this protection under the *Corporations Act 2001* (Cth).

An officer and a company director may have a civil and criminal liability under the *Corporations Act 2001* (Cth).³⁷⁵ Where directors have contravened their general duties under part 24D, a court may make a civil penalty under Part 9.4 the *Corporations Act 2001* (Cth). Further, where directors have breached a duty of solvency, they will be liable to pay compensation to the company³⁷⁶ or creditors.³⁷⁷ The court has the power to relieve a director from liability of a civil penalty provision by having regard to all the circumstances and where a person acted honestly.³⁷⁸

Moreover, a director may face criminal liability in relation to contravening the following obligations:

- failure to exercise their duties in good faith in a manner that is reckless or with intentional dishonesty;³⁷⁹
- abuse their position and information in a dishonest manner;³⁸⁰ and
- failure to cease trading when the company was insolvent.³⁸¹

4.4.3 Legal Status

Once a company is registered under the *Corporations Act 2001* (Cth), the company will then come into existence.³⁸² The company is a body corporate, which is an incorporated legal entity

³⁷³ *Corporations Act 2001* (Cth) s 9.

³⁷⁴ *Corporations Act 2001* (Cth) ss 517, 518.

³⁷⁵ Chapter five of this thesis provides an analysis of a company director's duties.

³⁷⁶ *Corporations Act 2001* (Cth) s 1317H.

³⁷⁷ *Corporations Act 2001* (Cth) s 588G(2).

³⁷⁸ *Corporations Act 2001* (Cth) s 1317S(7).

³⁷⁹ *Corporations Act 2001* (Cth) s 184(1).

³⁸⁰ *Corporations Act 2001* (Cth) s 184(2)–(3).

³⁸¹ *Corporations Act 2001* (Cth) s 588G(3).

³⁸² Registration will take place with ASIC. *Corporations Act 2001* (Cth) s 119.

with perpetual succession recognised in law.³⁸³ Therefore, like an incorporated association, a company limited by guarantee has the power to enforce rights by suing or being sued by others, incur liabilities, and acquire property in the entity's name.³⁸⁴

4.4.4 *Membership Entry and Rights*

The company will admit members upon those persons satisfying the conditions for membership, which are set out in the company's constitution.³⁸⁵ The relationship between the members and the company is based on the contract in the constitution.³⁸⁶ Furthermore, individuals must be prepared to become members of the company and have their names entered onto the register of members.³⁸⁷ Unlike an incorporated association legislation that stipulates a minimum number of members, this requirement is more relaxed for a company limited by guarantee, which requires only one member.³⁸⁸

4.4.5 *Rules*

Generally, a company's constitution outlines the rules on matters such as the conduct of the directors and shareholders, meetings, power of directors, and director's remuneration.³⁸⁹ Under the *Corporations Act 2001* (Cth), these rules govern the company's internal administration and management and are referred to as 'replaceable rules'.³⁹⁰ A company may replace or modify any or all of the replaceable rules.³⁹¹ Many of the replaceable rules, such as those dealing with shareholders, are not applicable to a company limited by guarantee. Therefore, it would be appropriate for the internal management of a company limited by guarantee to be governed by its a constitution and some of the replaceable rules.³⁹²

³⁸³ *Corporations Act 2001* (Cth) s 57A.

³⁸⁴ Lipton, Herzberg and Welsh, *Understanding Company Law* (Thomas Reuters, 16th ed, 2012) 23.

³⁸⁵ Harold Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 11th ed, 2013) 1021.

³⁸⁶ *Corporations Act 2001* (Cth) s 140(1).

³⁸⁷ *Corporations Act 2001* (Cth) s 231(b).

³⁸⁸ *Corporations Act 2001* (Cth) s 114.

³⁸⁹ Lipton, Herzberg and Welsh, *Understanding Company Law* (Thomas Reuters, 16th ed, 2012) 87.

³⁹⁰ *Corporations Act 2001* (Cth) s 141.

³⁹¹ *Corporations Act 2001* (Cth) s 135(2).

³⁹² Lipton, Herzberg and Welsh, *Understanding Company Law* (Thomas Reuters, 16th ed, 2012) 85.

4.4.6 *Source of Revenue*

A company limited by guarantee is prohibited from raising funds through activities that would require disclosure to investors, such as offering shares or debentures.³⁹³ This leaves a company limited by guarantee to undertake traditional revenue-making sources, such as donations, subscriptions, social activities, and government service delivery contracts.³⁹⁴

4.4.7 *Management Committee*

A company limited by guarantee is registered as a public company and, at the very least, it must have three directors and one secretary.³⁹⁵

4.5 Conclusion

There are a variety of forms that a not-for-profit organisation may choose to pursue altruistic missions and values, and the law treats each form differently. Regardless of the form, a not-for-profit organisation functions on the collective action of its members and/or volunteers. The collective action of its members is the most appealing feature of a not-for-profit organisation, and members serve their organisation in accordance with its rules and legislative provisions that support the achievement of the organisation's objectives. Furthermore, the law offers volunteers some immunity from liability through the CLA.

³⁹³ *Corporations Act 2001* (Cth) s 113(3).

³⁹⁴ Chapter Eight of this thesis analyses the role of not-for-profit organisations have in delivery services through government contracts.

³⁹⁵ Australian Securities and Investments Commission, *Registering not-for-profit or charitable organisations* <<http://www.asic.gov.au/asic/asic.nsf/byheadline/Registering+not-for-profit+or+charitable+organisations>>.

CHAPTER 5: Legal Duties as Part of the Governance Framework

*We do not have to be a Gandhi, or a Martin Luther King Jr., or a Nelson Mandela, or a Desmond Tutu, to recognise that we can have aims or priorities that differ from the single-minded pursuit of our own well-being.*³⁹⁶

5.0 Introduction

All forms of not-for-profit organisations are not immune from collapse due to mismanagement.³⁹⁷

In spite of an altruistic mission at its core, when a not-for-profit organisation does collapse, questions are inevitably raised regarding the degree of regulation these organisations can rely on in their management structure. In the push for improved regulation and greater governance, there is the misconception that officers of a management committee of an incorporated association find themselves in the same position as company directors.³⁹⁸ While this is true of officers of a company limited by guarantee it is not true otherwise.

Reliance on, and attraction to, this misconception is largely due to the slim body of case law and legislation for incorporated associations, which inadequately clarifies legal duties for its management committee.³⁹⁹ This chapter briefly examines the functions of a management

³⁹⁶ Amartya Sen, *The Idea of Justice* (Allen Lane, 2009) 18.

³⁹⁷ For example, Zoe's Place was placed into voluntary administration and was placed under investigation by the Health Quality and Complaints Commission for serious allegations relating to complaints of malpractice. Sophie Elsworth, 'Zoe's Place in Queensland may Close', *The Australian* (online), 18 June 2009 < <http://www.theaustralian.com.au/news/zoes-place-in-queensland-may-close/story-0-1225737048892>>. See also Kim Weinert, 'Is there a Perfect Environment to Allow a Villain and a Villainess to Thrive?' in Rachel Franks and Susan Meindl (eds), *The Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 49.

³⁹⁸ Keith Fletcher, *The Law Relating to Non-Profit Associations in Australia and New Zealand* (Law Book Company, 1986) 289; Andrew Twaits, 'The Duties of Officers and Employees in Non-Profit Organisations' (1998) 10(2) *Bond Law Review* 313; A. S. Sievers, *Associations and Clubs Law in Australia and New Zealand* (Federation Press, 2nd ed, 1996) 21.

³⁹⁹ There are two obvious reasons why there is a lack of judicial authority for incorporated associations. First, in the event a member of a Queensland incorporated association has a grievance regarding the misgivings of the management committee, all complaints must be settled by the Supreme Court. *Associations Incorporation Act 1981* (Qld) s 71(2). Supreme Court actions would be out of reach for an ordinary member (particularly for members of a level 1 and level 2 associations) due to high litigation costs and the risks in pursuing litigation, and the highly legalistic nature of making an application in this jurisdiction. Moreover, the Supreme Court has the discretionary power to dismiss applications if the court believes the matter is trivial. *Associations Incorporation Act 1981* (Qld) s 73(2)(a); See *Re Maggacis* [1994] 1 Qd R 59. Furthermore, Queensland's governing executive department (Office of Fair Trading) has no statutory authority to receive, investigate, or settle any complaints or disputes relating to the management of an incorporated association. The only powers the executive has over

committee as compared to a board of directors, and asserts that a need exists to regulate a committee member's conduct through legal duties.

Furthermore, Chapter Five compares each of the statutory legal duties of both a corporation and an incorporated association, illustrating the differences in the legal duties of a committee member as compared to a company director and how the law considers them differently.⁴⁰⁰ Precision can be seen to be lacking in both the common law and the statute law's approach to prescribing legal duties for a committee member. Consequently, to fill this gap, attention is turned to equity and the question of whether or not fiduciary principles can provide clarity.

Australia's development of fiduciary law in this area has stagnated with the courts expressing a reluctance to expand the established categories of fiduciary relationships and, also, to find for a breach of these duties within these established fiduciary categories. The application of this law to unincorporated and incorporated associations is largely unknown and previously unexamined. Chapter Five considers whether committee members of an unincorporated and an incorporated association are, in fact, fiduciaries through the established relationship of principal and agent and, therefore, subject to fiduciary duties.

5.1 The Respective Functions of a Board of Directors and a Management Committee

Similarities between the roles of a director and an officer of a management committee can be evidenced in that each operate as a collective group of individuals elected or appointed to their respective positions. The incorporated association legislation provides that the function of the management committee is to control and manage the association's operation and business; collectively, the committee has control of the association's property.⁴⁰¹ However, little is really known about how a management committee carries out these legislative functions. With no direct

incorporated association relates to the administration of an incorporated association. *Associations Incorporation Act 1981* (Qld) pt 6, div 2; *Associations Incorporation Regulations 1999* (Qld) reg 14 and pt 5 div 3.

⁴⁰⁰ The *Australian Charties and Not-for-Profit Commission (Consequential and Transitional) Act 2012* (Cth) turns off the statutory duties of care and diligence, good faith and not to misuse position or information under the *Corporations Act 2001* (Cth) for directors of a company limited by guarantee. Therefore, it is prudent to note that this Chapter is concerned with the legal duties of a director within a for-profit entity.

⁴⁰¹ *Associations Incorporation Act 1981* (Qld) s 60; *Associations Incorporation Act 1964* (Tas) s 21 and Model Rule 23; *Associations Incorporation Act 1984* (NSW) s 21; *Associations Regulations 2004* (Model Constitution) (NT) pt 4; *Associations Incorporation Act 1981* (Vic) sch 1 r 4 (Vic); *Associations Incorporation Act 1985* (SA) s 29; *Associations Incorporation Act 1987* (WA) s 20; *Associations Incorporation Act 1991* (ACT) s 60. Furthermore, an association's property also includes the association's funds as well as real property.

prescription (either by convention or legislation) on how to achieve these functions and manage an association, a management committee has the freedom and the autonomy on how best to manage its association. There is, of course, an expectation that a management committee will guide the management of the association in accordance with the association's altruistic mission – that is, with integrity, and in a manner free from self-interest and, moreover, impropriety

The pursuit of profit maximisation for companies provides a more definitive set of functions of a board of directors:

- appointing and rewarding a chief executive officer;
- setting business goals;
- formulating strategies;
- approving business plans (which includes setting annual budgets, make key management decisions such as, major capital expenditure, restructuring and refinancing and business acquisitions);
- monitoring the performance and results of the business and management;
- establishing and review shareholders policies (where relevant); and
- examining conformance strategies.⁴⁰²

These tasks, both specific and numerous, clearly dictate that a board of director's function is to achieve and maintain a company's fiscal capabilities. Accordingly, the economic nature of a company's activities is justification for regulation, and for a company director to be accountable. However, the traditional view is that incorporated associations pursue non-economic activities, and that the trustworthiness of an incorporated association means the need for regulation is not warranted. Without regulation, or a clear set of obligations compelling an officer to undertake the proper administration of a not-for-profit organisation, dishonest committee members are free to use the incorporated association's property and resources for private interests and gain.⁴⁰³

⁴⁰² Horald Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 15th ed., 2013) 225-226.

⁴⁰³ Kim Weinert, 'Is There a Perfect Environment for a Villain and Villainess to Survive?' in Rachel Franks and Susan E. Meindi (eds), *The Real and Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012).

5.2 Regulation and Accountability of Committee Members

There are overwhelming social and economic reasons to justify the regulation of not-for-profit organisations. While theoretically both an incorporated association and a company are accountable to their members, a company achieves this better than an incorporated association. Corporation law promotes a culture of transparency and accountability through the concept of governance. Basic governance within a corporation provides a framework to protect an organisation's resources, and to effectively manage and control risk.⁴⁰⁴ The governance framework for a company is set by the law and reinforced by regulatory bodies.⁴⁰⁵ The requirements compel a company to maintain robust internal processes and have systems in place, such as accurate financial reporting, and timely disclosure of material interests.⁴⁰⁶ At the centre of the governance framework is the board of directors and, specially, attention is on the director's behaviour in governing the organisation. In undertaking their roles, directors must follow specific legal duties and obligations, which is an important mechanism of organisational governance.⁴⁰⁷ Conversely, the law relating to incorporated associations does very little to encourage a management committee to achieve transparency, accountability, governance, or to protect an association's property.

5.3 The Regulatory Framework

5.3.1 Statutory Duties

For management committees of an incorporated organisation the duties are set out in the state legislation. Directors of a company limited by guarantee are subject to the *Corporations Act 2001* (Cth). The *Corporations Act 2001* (Cth) provides statutory duties extending to: each director; company secretary; any other person who makes or participates in decision-making that affects the whole or a substantial part of the company; and anyone else who has the capacity to

⁴⁰⁴ Adrian Cadbury, *Corporate Governance and Chairmanship: A Personal View* (Oxford University Press, 2002) 220.

⁴⁰⁵ Alan Calder, *Corporate Governance: A Practical Guide to the Legal Frameworks and International Codes of Practice* (Kogan Page, 2008) 1.

⁴⁰⁶ *Corporations Act 2001* (Cth).

⁴⁰⁷ Ian Ramsay, *Corporate Governance and the Duties of Company Directors*, *Centre for Corporate Law and Securities Regulation*, Faculty of Law (University of Melbourne, 1997) 10.

significantly affect the company's financial standing.⁴⁰⁸ The incorporated associations' legislation does not have a similar statutory provision; however, any statutory duties prescribed under the associations legislation are read to apply only to members of a management committee.⁴⁰⁹ There are numerous inconsistencies between the statutory duties of a company director and an officer of a management committee, and each duty will be individually examined.

5.3.2 *Duty of Care and Diligence*

Section 180(1) of the *Corporations Act 2001* (Cth) provides that directors must discharge their duties and use their powers with a degree of care and diligence that a reasonable person would exercise if they were in the position and in those same circumstances. A similar, clearly expressed provision in the legislation for incorporated associations can be found in Victoria and South Australia, where this provision states that an officer of a management committee must act at all times with reasonable care and diligence when exercising their powers and in discharging their duties of their office.⁴¹⁰ The wording of this provision is similar to the *Corporations Act 2001* (Cth); however section 39A(4) of the South Australian Act and the new Victorian legislation does not go as far as section 180(1) because they omit the key phrases: 'in a like position'; and 'in the corporation's circumstances'. The exclusion of these means this provision does not import any standard of care and diligence (whether objective or subjective) on an officer of a management committee.

The cases tend not to distinguish clearly between duties of care, diligence and skill. The duty of diligence first appeared in the case of the *Charitable Corporation v Sutton* (1742) 2 Atk 400 (citing *Coggs v Bernard* 1 Salk 26; 91 ER 25) and aspects of this case have been referred to in modern cases. Although it can be argued that the duty of diligence is a sub-set of care, due to the loose usage in the cases it is worth considering it separately.

⁴⁰⁸ *Corporations Act 2001* (Cth) s 180(1). Section 9 of the *Corporations Act 2001* (Cth) defines the term 'director' to also include *de facto* and shadow directors.

⁴⁰⁹ See *Associations Incorporation Act 2009* (NSW) pt 4, dv 1; *Associations Incorporation Act 1995* (SA) pt 4, dv 1; *Associations Incorporation Act 1981* (Vic) pt v; *Associations Incorporation Act 1997* (WA) pt v; *Associations Act 2003* (NT) pt 4, dv 1; *Associations Incorporation Act 1991* (ACT) pt 4.

⁴¹⁰ *Associations Incorporation Act 1985* (SA) s 39A; *Associations Incorporation Reform Act 2012* (Vic) s 84; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 45(3)

5.3.3 *The Duty of Skill*

The elements of skill and a standard of skill are not specified in either section 39A(4) of *Associations Incorporation Act 1995* (SA) or section 180(1) of the *Corporations Act 2001* (Cth). However, over time, the courts have inferred that directors are subject to an objective standard that obliges directors to:

- reasonably understand the company's affairs insofar that a director is capable of reaching an informed opinion of the company's financial position;⁴¹¹
- be capable to keep abreast of the company's affairs;⁴¹² and
- to keep sufficient abreast of the company's affairs to act appropriately in the event the company is unable to pay its debts in due course, and the director is to reasonably expect the company cannot pay its debt.⁴¹³

The payment of debts is addressed by three states in their respective association's legislation: New South Wales, Northern Territory, and South Australia. These provisions refer to a member of the management committee, or a person who took part in the management of the association, who at the time of, or immediately before, incurring a debt had reasonable grounds to accept that the association would be capable of paying the incurred debt when it became due.⁴¹⁴ Furthermore, the states' legislation provides a statutory defence if an officer can prove the debt was incurred outside of their consent and authority.⁴¹⁵ Additionally, officers will not be liable if, at the time the debt was incurred, they had reasonable cause to accept that the association could not pay all its debts when they became due.⁴¹⁶ These provisions imply that a committee member must have knowledge and a basic understanding of the association's finances. Company directors are required to possess a level of skill to be able to understand the company's affairs and its financial statements.⁴¹⁷

⁴¹¹ *Statewide Tobacco Services v Morley* (1990) 2 ACSR 405.

⁴¹² *Re Australasian Venzolana Pty Ltd* (1962) 4 FLR 60.

⁴¹³ *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115.

⁴¹⁴ *Associations Incorporation Act 2009* (NSW) s 68; *Associations Act 2003* (NT) s 90; *Associations Incorporation Act 1985* (SA) s 9AD.

⁴¹⁵ *Associations Incorporation Act 2009* (NSW) s 68(3); *Associations Act 2003* (NT) s 90(2); *Associations Incorporation Act 1985* (SA) s 49AD(2).

⁴¹⁶ *Associations Incorporation Act 2009* (NSW) s 68(3); *Associations Act 2003* (NT) 90(2); *Associations Incorporation Act 1985* (SA) s 49AD(2).

⁴¹⁷ Harold Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 15th ed, 2013) 501.

5.3.4 *Duty of Solvency*

Under the provisions of the *Corporations Act 2001* (Cth), a company director has a duty to prevent insolvent trading.⁴¹⁸ New South Wales and the Northern Territory also place a positive duty to prevent insolvency upon committee members, similar to that of company directors. Furthermore, the legislation of these states has defence and penalty provisions that reflect sections 588H (defence) and 588J (penalty and recovery of the debt) of the *Corporations Act 2001* (Cth).

While these respective provisions for the prevention of insolvency employ different terms, there is a defence available for a director and a committee member if both are able to prove that they had reasonable grounds, or a reasonable presumption, to expect the association or company could meet its debts at a time, or shortly after, the debt was incurred.⁴¹⁹ Looking specifically at the key term ‘reasonable grounds to expect’, which is contained in both pieces of legislation, it implies that there was a possibility that the debt could be paid.⁴²⁰ Therefore, there must have reasonable grounds of being confident that the company is solvent.⁴²¹ Further, committee members in New South Wales and the Northern Territory could successfully argue that an officer of a management committee had reasonable grounds to expect the association was solvent.

5.3.5 *Duty of Diligence*

For a company director, ‘their duty of care is their obligation to exercise reasonable prudence.’⁴²² A director in exercising this duty must not be seen to be passive in attending board meetings.⁴²³ The common law expects company directors to attend all meetings unless there are exceptional circumstances that prevent them from attending.⁴²⁴ However, for a committee member of an incorporated association, the requirement to attend meetings is less stringent than that of a corporation, and is largely subject to association’s *Model Rules*. Queensland’s *Model Rules* set

⁴¹⁸ *Corporations Act 2001* (Cth) s 588G.

⁴¹⁹ *Corporations Act 2001* (Cth) s 588H(2); *Associations Incorporation 2009* (NSW) s 68(3); *Associations Act 2003* (NT) s 90(2).

⁴²⁰ *Tourprint International Pty Ltd (in liq) v Bott* (1999) 17 ACLC 1543.

⁴²¹ *Metropolitan Fire Systems Pty Ltd v Miller* (1997) 23 ASCR 699.

⁴²² *Re Property Force Consultants Pty Ltd* (1995) 13 ACLC 1501, 1061.

⁴²³ *Vrisakis v ASIC* (1993) 9 WAR 395.

⁴²⁴ *Vrisakis v ASIC* (1993) 9 WAR 395.

out the required number of members, and who from the management committee must be present, to conduct meetings⁴²⁵ – but these *Rules* places no specific obligation on individual members as to their rate of attendance. Conversely, the chair of meetings must be the association’s president of the association, which gives the implication that there is a higher requirement on the president to attend meetings more than other committee members.⁴²⁶ Furthermore, McPherson J in *Ward v Eltherington* held that an officer could not avoid liability by being absent from all committee meetings.⁴²⁷

Additionally, a director’s inattention at board meetings is a cause for concern.⁴²⁸ The concept of attendance, as it applies to a company director, has been stated as taking the reasonable steps to guide and monitor the company with attention to:⁴²⁹

1. acquire a rudimentary understanding of the company’s business;
2. be informed about the company’s activities;
3. generally monitor the company’s affairs and policies; and
4. be familiar with the financial status of the company by undertaking regular review of the company’s financial statements.⁴³⁰

For incorporated associations, there are no guiding principles or statutory provisions applicable to committee members on the obligation of being attentive at meetings. As the statutory power and responsibility is given to committee members to manage an association, there is a reasonable expectation that a committee member would be conscientious of the association’s activities, policies, affairs and its financial standing.

⁴²⁵ *Associations Incorporation Regulation 1999* (Qld) pt 3, div 1, Model Rule 23(5). Queensland’s *Model Rules* require that for a management committee to be held, more than 50 per cent of elected members to the committee must be present. *Associations Incorporation Regulation 1999* (Qld) pt 3, div 1, Model Rule 24.

⁴²⁶ *Associations Incorporation Regulation 1964* (Tas) Model Rule 15; *Associations Incorporation Regulation 1984* (NSW) Model Rule 8; *Associations (Model Constitution) Regulations 2005* (NT) model rule 35; *Associations Incorporation Regulations 1998* (Vic) Model Rule 14; *Associations Incorporation Regulation 1999* (Qld) reg 23(9) and Model Rule 14. Associations can determine their own committee meeting procedure and the numbers for a quorum. These provisions also provide for the incorporated association to have alternatives for a chair should the president be unable to attend. *Associations Incorporation Act 1985* (SA) s 23A(1)(c)(v); *Associations Incorporation Act 1987* (WA) s 16, sch 1; *Associations Incorporation Act 1991* (ACT) sch 1.

⁴²⁷ [1982] Qd R 561.

⁴²⁸ *Ashurst v Mason* (1875) LR 20 Eq 225.

⁴²⁹ *Daniels t/as Deloitte Haskins Sells v AWA Ltd* (1995) 37 NSWLR 438.

⁴³⁰ *Francis v United Jersey Bank* (1981) 432A 2d 414; *Daniel t/as Deloitte Haskins Sells v QWA Ltd* (1995) ACRS, 666-667.

5.3.6 *Reliance and Delegation*

Both a company director and a committee member could find themselves in circumstances where they need to rely on advice (expert or otherwise) and delegate roles to others within the corporation or association. The management committee has the legislative ability to delegate any or all of their functions and powers to a subcommittee of the association.⁴³¹ A company's board of directors also have the statutory authority to delegate their powers.⁴³² Excluding the Northern Territory, the delegation power for an incorporated association is largely confined to sub-committees, whereas directors can delegate their own powers to other directors, employees, or to any other persons.

The associations' legislation does not specify whether a management committee is ultimately responsible for the actions of the delegate, whereas the Commonwealth statute provides that a director who delegated power is responsible for the delegate.⁴³³ It is unclear whether such a responsibility falls onto the management committee and/or the individual. The issue of whether or not the rules of agency are applicable in this instance will be discussed further in this chapter.

Boards of directors have the power to rely on and seek advice from certain people.⁴³⁴ Information and professional advice is often sought and relied on by directors, and they would have reasonable grounds for having confidence in the following people:

- *An employee of the corporation* – grounds for confidence: the information given is reliable and competent in relation to matters concerned; or
- *A professional advisor or expert* – grounds for confidence: the information given is regarded to be within the person's professional or expert competence; or

⁴³¹ *Associations (Model Constitution) Regulations 2004* (NT) reg 25; *Associations Incorporation Act 1964* (Tas) s 28; *Associations Incorporation Regulation 2010* (NSW) sch 1, Model Rule 21; *Associations Incorporation Regulation 1999* (Qld) reg 27; *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 43. South Australia, Western Australia and the Australian Capital Territory have no express provisions that allows for the management committee to delegate powers to a sub-committee. Alternatively, a management committee maybe capable of creating and delegating to a sub-committee as the legislation in these jurisdictions provides for the ability of the association to alter the constitution or rules, and this would see the creation of sub-committees. The altered rules may go so far as to state the sub-committee's purpose, responsibility and powers.

⁴³² *Corporation Act 2001* (Cth) s 198D.

⁴³³ Directors will not be liable if they believed, on reasonable grounds, that the delegate would exercise their power, which is in line with the duties of the company's directors, as required by law, the company's constitution, and in good faith – providing the director made proper inquiry that the delegate was reliable and competent. *Law Economic Reform Program Act 1999* (Cth) s 190 (1)-(2).

⁴³⁴ *Corporations Act 2001* (Cth) s 189.

- Another *director or officer* – grounds for confidence: matters that are within the director’s or officer’s authority; or
- A *committee of directors* – grounds for confidence: matters within the committee’s authority, and on which the director did not serve in relation to such matters.⁴³⁵

To determine whether or not a director or an officer holder within a Victorian incorporated association has performed a duty of care and diligence under the general law and statute, it must be shown that the director’s reliance was in good faith.⁴³⁶ For a director’s reliance to be reasonable, a director should: make an independent assessment of the information or advice; have their own knowledge of the corporation’s operation; have knowledge of the company’s and the corporation’s complex structure;⁴³⁷ and, that their reliance on the information or advice can be said to be reasonable.⁴³⁸

Section 189 provides a safe harbour for directors to rely on the information or advice from others without verification.⁴³⁹ This presumption is rebuttable if a director knew, or by the exercise of their ordinary care should have known, that any facts or issues would not be reasonable.⁴⁴⁰ The general law will also look at the transaction’s risk and its nature, and the steps taken by the director as to the reasonableness of the reliance.⁴⁴¹

The legislative requirement for directors to undertake an independent assessment of the information or advice requires directors to do more than listen. They must assess the information or advice provided, and employ their skill and judgment.⁴⁴² The criticism aimed at this legislative requirement is that it encourages directors to act alone instead of working as a collective, which is how a board should operate.⁴⁴³

Section 588H and the Victorian Act provide a defence for directors and Victorian office holders within an incorporated association if they can prove that they relied on information about

⁴³⁵ *Corporations Act 2001* (Cth) s 189(a)(i)-(iv).

⁴³⁶ *Associations Incorporation Reform Act 2012* (Vic) s 86(2)(b); *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 45(4)(a).

⁴³⁷ *Corporations Act 2001* (Cth) s 189(b)-(c); *Associations Incorporation Reform Act 2012* (Vic) 86(2)(b)(ii).

⁴³⁸ *Corporations Act 2001* (Cth) s 189(c).

⁴³⁹ *Australian Securities and Investments Commission v Adler* (2002) 41 ACSR 72.

⁴⁴⁰ *Daniels v Anderson* (1995) ACSR 665-6.

⁴⁴¹ *Adler v ASIC* (2003) 46 ACSR 504.

⁴⁴² *Southern Resources Ltd v Residues Treatment Trading Co Ltd* (1990) 59 SASR 455.

⁴⁴³ John Farrar, *Corporate Governance – Theories, Principles and Practice* (Oxford University Press, 3rd ed, 2008) 98.

the company's affairs provided to them from a competent person.⁴⁴⁴ However, directors cannot rely upon this defence if they have failed in their duty to prevent the company's insolvent trading, or by inadequately performing their general law and statutory duties.⁴⁴⁵ A director's failings would be a lack of participation in the company's affairs,⁴⁴⁶ or the unreasonable reliance on other directors to look after the affairs of the company.⁴⁴⁷ Should a director not give the sufficient information to a person needing to perform the task that that director wishes to rely upon, then a section 588H defence would not be available.⁴⁴⁸

The statutory reliance for committee members of incorporated associations is only available in South Australia and in Victoria. Section 39AB⁴⁴⁹ is almost an exact reflection of section 189 of the *Corporations Act 2001* (Cth), the only point of difference being that a South Australian association may rely on a sub-committee of association's members, whereas a company a director and an officer holder within a Victorian incorporated association can rely on information or advice from others, such as an expert, an employee, and other directors.⁴⁵⁰ The provisions on reliance for associations in South Australia and Victoria are straightforward, but for all the other Australian jurisdictions there is statutory silence.

Despite this silence, it is arguably open to a management committee, in those jurisdictions without reliance provisions, to search out and rely on information and professional/expert advice to assist them in the proper administration of the association – and, moreover, to protect the association's property.

5.3.7 *The Duty of Acting in Good Faith, in the Best Interest and for Proper Purpose*

This all-encompassing statutory duty focuses on different elements of 'acting in good faith, in the interest of the company for proper purpose'. Section 181 and section 85 of the *Associations Incorporation Reform Act 2012* (Vic) requires that directors and other officers must exercise their powers and discharge their duties in good faith, in the best interest of the corporation and the

⁴⁴⁴ *Corporations Act 2001* (Cth); *Associations Incorporation Reform Act 2012* (Vic) s 86(2)(a)(i)-(iv).

⁴⁴⁵ *Corporations Act 2001* (Cth) s 588G.

⁴⁴⁶ *Australian Securities and Investments Commission v Plymin* [No 1] (2003) 175 FLR 124.

⁴⁴⁷ *Metal Manufacturers Ltd v Lewis* (1988) 13 NSWLR 315.

⁴⁴⁸ *Manpac Industries Pty Ltd v Ceccattini* (2002) 20 ACLC 1304.

⁴⁴⁹ *Associations Incorporation Act 1985* (SA).

⁴⁵⁰ *Corporations Act 2001* (Cth) s 189(a)(iv); *Associations Incorporation Act 1985* (SA) s 39AB (a)(iv); *Associations Incorporation Reform Act 2012* (Vic) s 86.

association, and for a proper purpose.⁴⁵¹ The duties to act in good faith and in the interest of the company are viewed as a fundamental civil obligation for a director.⁴⁵² How the courts test a contravention of this section is by objective standards based on what a comparable person, with the same knowledge and skills as the director, would have done in the same circumstances.⁴⁵³ The rules regarding best interest and proper purpose are discussed in detail below.

5.3.7.1 *Best Interest*

The best interest of the company may be defined by the company's constitution, which would affect a director's duties,⁴⁵⁴ and is generally linked to the best interests of the shareholders as a general body.⁴⁵⁵ In circumstances where different classes of shareholders have diverging interests, a director must act fairly between the different classes.⁴⁵⁶ These classes of shareholders under the corporation's constitution allow the board to take into account the interests of one group over another member group or, creditor.⁴⁵⁷ For an incorporated association, the management committee could be required to advance its objective that it is non-commercial.

Overall, incorporated associations must pursue their altruistic objectives, which serve as an association's best interest. Similar to a company, an incorporated association allows for different groups of members, such as financial, associate, or social members. Financial or active members confer voting rights, whereas social or associate members do not have voting rights and are confined to the enjoyment of the association's facilities. Unlike a company director, a management committee is not required to take into account the

⁴⁵¹ *Corporations Act 2001* (Cth). See also *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 45(4)(b).

⁴⁵² H. Ford, R. Austin and I. Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 15th ed., 2013) 513. The Note contained in section 85 of the *Associations Incorporation Reform Act 2012* (Vic) states that it has the same effect and application as section 146 of the *Corporations Act 2001* (Cth). Should an officer holder within a Victorian incorporated association contravene section 85 the guilty person may be ordered by a court to pay a pecuniary penalty of up to \$20,000.

⁴⁵³ *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821.

⁴⁵⁴ *Whitehouse v Carlton Hotel Pty Ltd* (1987) 162 CLR 285.

⁴⁵⁵ *Mills v Mills* (1938) 60 CLR 150.

⁴⁵⁶ *Mills v Mills* (1938) 60 CLR 150.

⁴⁵⁷ Harold Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 14th ed, 2010) 381.

interests of one group of members over another group.⁴⁵⁸ The caution here for management committees and the board of directors is that a departure from the rules or constitution may result in their treatment towards members being seen as oppressive and unfairly prejudicial or discriminatory to a specific group or class of members.⁴⁵⁹

5.3.7.2 *Proper Purpose*

The element of proper purpose under section 181(1)(d) of the Corporations Act⁴⁶⁰ requires directors and other officers to exercise their powers and discharge their duties for a proper purpose.⁴⁶¹ For a company director, this is conferred by contract and legislation to exercise their powers for the expressed or implied purpose.⁴⁶² The ‘proper purpose’ doctrine for a company director is a set of principles, which determines if a director has acted for an improper purpose:⁴⁶³

- the fiduciary powers of directors are to be exercised for the purpose for which they are given, not collateral purposes;
- the substantial purpose of directors was improper or collateral to the director’s duties;⁴⁶⁴
- the acts performed by a director were for the benefit of the company;⁴⁶⁵ and
- the court will apply the ‘but for’ test to determine what the director’s relevant purpose was (i.e. the court will consider if a director would still have acted in the same manner had the collateral purpose not existed).⁴⁶⁶

The element of proper purpose for a committee member would be to achieve the association’s objectives conferred upon them by the association’s rules and respective legislation. The absence of any provisions contained in the association’s legislation across

⁴⁵⁸ *Wayde Anor v New South Wales Rugby League Ltd* (1985) 61 ALR 225; *Melbourne Juventus Soccer Club v Australian Soccer League Ltd*, Federal Court of Australia, Melbourne, Onley J, 20 September 1995.

⁴⁶⁰ *Corporations Act 2001* (Cth); *Gambotto v WCP Ltd* (1995) 127 ALR 417.

⁴⁶¹ Section 181 is a civil provision, whereas section 184 is a criminal provision for a director’s duty of good faith within the *Corporations Act 2001* (Cth).

⁴⁶² Harold Ford, Robert Austin and Ian Ramsay, *Ford’s Principles of Corporations Law* (Butterworths, 14th ed, 2010) 400–401.

⁴⁶³ *Permanent Building Society (in liq) v Wheeler* (1994) 14 ASCR 109.

⁴⁶⁴ The determination is not whether director’s decisions were bad or good, but whether they acted in breach of their fiduciary duties. *Permanent Building Society (in liq) v Wheeler* (1994) 14 ASCR 109.

⁴⁶⁵ This standard of testing for these principles is not whether the director acted honestly or altruistically. A director’s conduct will be objectively assessed. *Australian Securities and Investments Commission v Adler* (2002) 168 FLR 253.

⁴⁶⁶ *Whitehouse v Carlton Hotel Pty Ltd* (1987) 162 CLR 294 (Mason, Deane and Dawson JJ).

the jurisdictions, knowing whether or not there is a duty to act for proper purpose upon a management committee, is unclear.

5.3.8 *The Duty Not to Improperly Use a Position or Information*

This duty requires a company director, an officer and an employee not to improperly use a position. For a company director this duty is a civil obligation under 182(1) of the *Corporations Act 2001* (Cth) and they must not improperly use their position to:

- a) gain an advantage for themselves or someone else; or
- b) cause detriment to the corporation.

This provision overlaps with section 183(1), which states that a corporation's director, officer or employee are prohibited to obtain information by virtue of their positions, and they must not use that information for a personal gain or an advantage for someone else, or to cause detriment to the corporation.⁴⁶⁷

Some incorporated associations have provisions for the duty not to misuse a position or information. However, the legislative framework varies between jurisdictions. In New South Wales, Australian Capital Territory and Victoria there is statutory duty not to improperly use information or a position, and these provisions apply to committee members and former committee members.⁴⁶⁸ However, in South Australia and the Northern Territory, this duty applies to officers, former officers and employees – which is the same under the *Corporations Act 2001* (Cth). Officers of incorporated associations in the Australian Capital Territory only have a duty not to improperly use their position.⁴⁶⁹

The provisions for misuse of information and position for incorporated associations in each jurisdiction uses the phrase 'to gain, directly or indirectly, any pecuniary benefit or material advantage for himself or herself or any other person, or so as to cause a detriment to the association.'⁴⁷⁰ This phrase for incorporated associations is similar to the phrase that applies to corporations. For corporations, this phrase is found in section 184(2)(a), which is a criminal

⁴⁶⁷ *Corporations Act 2001* (Cth).

⁴⁶⁸ *Associations Incorporation Act 2009* (NSW) ss 32-33; *Associations Incorporation Act 1981* (Vic) s 29A; *Associations Incorporation Reform Act 2012* (Vic) s 83. See also *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 45(5).

⁴⁶⁹ *Associations Incorporation Act 1991* (ACT) s 111(1).

⁴⁷⁰ *Associations Incorporation Act 1985* (SA) s 39A(3); *Associations Act 2003* (NT) s 33(2)-(3).

provision. Apart from New South Wales, the statutes for incorporated associations have not separated these provisions into civil obligations or criminal offenses like the *Corporations Act 2001* (Cth).

The duties of a committee member differ between jurisdictions. The sections concerning the improper use of position for management committees in the Northern Territory, Victoria, South Australian and the Australian Capital Territory directly reflect section 182(1) for corporations, that is: not to improperly use their positions.⁴⁷¹ The other two jurisdictions, New South Wales and Victoria, have approached the improper use element in another way. Victoria's legislation states that members of the management committee must not knowingly or recklessly make improper use of their position in the association.⁴⁷² The words 'knowingly' or 'recklessly' imports that a committee member who contravenes this provision is conscious of the impropriety. The Victorian provision for the improper use of a position by a committee member follows the ruling in *R v Byrnes*,⁴⁷³ thus making the state of mind relevant when testing a contravention objectively.

New South Wales has taken a different approach to the improper use of a committee member's position. Under section 33, committee members are guilty if they use their position with intention of directly or indirectly gaining an advantage for themselves or others, or if they cause detriment to the association.⁴⁷⁴ The New South Wales provision follows the criminal offense of section 184(2)(a) within the *Corporations Act 2001* (Cth). However, New South Wales' provision does not contain the element of impropriety like the other jurisdictions and the *Corporations Act 2001* (Cth). Rather, this provision itself is concerned with intent and dishonesty. The consequences for breaching section 33⁴⁷⁵ replicates the same penalties for contravening section 184(2),⁴⁷⁶ which is imprisonment, a pecuniary penalty, or both.⁴⁷⁷ The New

⁴⁷¹ *Corporations Act 2001* (Cth); *Associations Act 2003* (NT) s 33(3); *Associations Incorporation Act 1985* (SA) s 39A(3); *Associations Incorporation Act 1991* (ACT) s 111(1).

⁴⁷² *Associations Incorporation Act 1981* (Vic) s 29A(2); *Associations Incorporation Reform Act 2012* (Vic) s 83(4).

⁴⁷³ (1995) 130 ALR 529.

⁴⁷⁴ *Associations Incorporation Act 2009* (NSW).

⁴⁷⁵ *Associations Incorporation Act 2009* (NSW).

⁴⁷⁶ *Corporations Act 2001* (Cth).

⁴⁷⁷ The New South Wales' legislators are sending a strong public policy message to deter committee members of acting dishonestly by imposing a criminal provision. *Associations Incorporation Act 2009* (NSW) s 33. The penalty for improperly using information or position is a civil penalty up to \$20,000, and a court may also order compensation to the effected incorporated association. *Associations Incorporation Reform Act 2012* (Vic) s 83(5).

South Wales provision closely resembles the fiduciary duty to act honestly, but it is the selection of the word ‘dishonesty’ that should be discussed further.⁴⁷⁸

Regardless of what term is employed – ‘improper’, or ‘dishonest use of a position’ – its reach and effect are alike. However, for New South Wales the application of section 33⁴⁷⁹ is narrower than the respective provisions for corporations and the jurisdictions of South Australia, the Northern Territory, and the Australian Capital Territory.⁴⁸⁰ Being found guilty of breaching this provision turns, and depends only, on the committee member’s awareness of the wrongdoing. This narrow provision fails to provide for circumstances where committee members have purportedly acted honestly, reasonably, and without any intention of harm or an advantage, but have misused their position.⁴⁸¹

5.3.9 *Duty Not to Improperly Use Information*

Section 183 of the *Corporations Act 2001* (Cth) states that a director, an officer, an employee who obtains information must not improperly use that information to gain an advantage for themselves or someone else,⁴⁸² or cause detriment to the company.⁴⁸³ The main concept in this provision is the term ‘information’. Information is referred as the type of information that the law of equity would restrict the director from using for a personal profit.⁴⁸⁴ Furthermore, a finding of improper use of information could be where a director has failed to consider the general interests of a creditor that caused detriment to the company.⁴⁸⁵ Breaching either of the impropriety provisions will attract civil⁴⁸⁶ and/or criminal penalties.⁴⁸⁷

Similarly, the statutory provisions relating to the misuse of position for incorporated associations are expressed as the improper use or dishonest use of information. There are only

⁴⁷⁸ *Phipps v Boardman* [1967] 2 AC 46.

⁴⁷⁹ *Associations Incorporation Act 2009* (NSW).

⁴⁸⁰ *Corporations Act 2001* (Cth) s 182; *Associations Incorporation Act 1985* (SA) s 39A(3); *Associations Act* (NT) s 33(3); *Associations Incorporation Act 1991* (ACT) s 111(1).

⁴⁸¹ *R v Towey* (1996) 21 ACSR 46, 61.

⁴⁸² *Corporations Act 2001* (Cth) s 183(1).

⁴⁸³ *Corporations Act 2001* (Cth) s 182(2).

⁴⁸⁴ *Rosetex Co Pty Ltd v Licata* (1994) 12 ACLC 269 (Young, J).

⁴⁸⁵ *McNamara v Flavel* (1988) 13 ACLR 619.

⁴⁸⁶ Civil penalties are in the forms of a pecuniary penalty order, disqualification order and or compensation order. Such orders are proved on the balance of probabilities that a contravention of sections 182 and 183 of the *Corporations Act 2001* (Cth).

⁴⁸⁷ *Corporations Act 2001* (Cth) s 214.

four jurisdictions that have express provisions within the incorporated associations' legislative framework: Victoria; South Australia; New South Wales; and the Northern Territory. The application of these provisions regarding the misuse of information varies between each jurisdiction. South Australia and the Northern Territory have provisions similar to, and are as wide as, those provisions found in the *Corporations Act 2001* (Cth); these apply to a current or former officer and employee of the incorporated association.⁴⁸⁸ However, in New South Wales and Victoria, the improper use of information only applies to current and former committee members of the management committee and not to employees.⁴⁸⁹

The Australian Capital Territory has similar provisions that overlap between the use of a position and information for members of a management committee. Three out of the four jurisdictions prohibit the misuse of information if it is 'acquired by virtue of their position'.⁴⁹⁰ This phrase is not expressed in the *Corporation Act 2001* (Cth), but it is one factor from a list in establishing a breach of section 183.⁴⁹¹ Santow J in *Forkserve Pty Ltd v Jack* listed a total of seven factors needed to prove that an officer of a corporation breached section 183 of the *Corporations Act 2001* (Cth)⁴⁹² – each one of these is directly embraced into the incorporated associations' statute for the jurisdictions of South Australia, the Northern Territory and Victoria.⁴⁹³

5.3.10 Duty to Disclose a Personal Interest

The statutory provisions regarding interested directors and members of a management committee stem largely from the conflict rule. The conflict rule, in general, prohibits directors placing themselves in a position where their personal interest or duty will conflict with their duty to the

⁴⁸⁸ *Associations Incorporated Act 1985* (SA) s 39A(2); *Associations Act* (NT) s 33(2); *Corporations Act 2001* (Cth) s 183(1),(4).

⁴⁸⁹ *Associations Incorporated Act 2009* (NSW) s 32; *Associations Incorporated Act 1981* (Vic) s 29A(1); *Associations Incorporation Reform Act 2012* (Vic) s 83(1). See also *Associations Incorporation Reform Regulations 2012* (Vic) sch 4, Model Rule 65, but this Rule is only applicable to current committee members.

⁴⁹⁰ *Associations Act* (NT) s 33(2); *Associations Incorporation Act 1981* (Vic) s 29A(1); *Associations Incorporation Act 1985* (SA) s 39A(2).

⁴⁹¹ *Corporations Act 2001* (Cth); *Forkserve Pty Ltd v Jack* (2000) 19 ACLC 299.

⁴⁹² (2000) 19 ACLC 299.

⁴⁹³ The statutory provision in Victoria for the improper use of information also contains the words 'knowingly or recklessly', which is consistent with the provision regarding the improper use of a position by a member of a management committee and the ruling in *R v Byrnes* (1995) 130 ALR 529.

company.⁴⁹⁴ However, applying this rule in its strictest form creates practical difficulties in a commercial setting, such as prohibiting a director from holding a board position, being a nominee director or a director being a shareholder. The courts have acknowledged these difficulties and have accepted that a director can act with a personal interest. However, this is prohibited if the personal interest is not a *bona fide* concern for the benefit of the whole company or fairness between members.⁴⁹⁵

For corporations, section 191(1) states that a director of a company with a material interest in a matter that relates to the affairs of the company must give notice to other directors of that interest unless section 191(2) says otherwise.⁴⁹⁶ There is strict liability by a director to notify other directors of a material interest when a conflict arises.⁴⁹⁷ Further, this provision applies to all directors, regardless of whether the company's constitution permits a director to be interested in a transaction with the company.⁴⁹⁸ The heart of this provision is that companies cannot allow themselves to diminish the general prohibition on conflicts by the company's constitution.

The term 'material personal interest' is not a term defined by the *Corporations Act*, and the common law is consulted as to its meaning.⁴⁹⁹ Specifically, the word 'material' requires an assessment of what a director personally expects and the matter being considered.⁵⁰⁰ This assessment looks at the nature of the interest and the director's capacity to influence the vote and decision/s by the board and whether the conflict of interest is of a real and substantial kind.⁵⁰¹

⁴⁹⁴ Harold Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 15th ed, 2013) 528.

⁴⁹⁵ *Mills v Mills* (1938) 60 CLR 150.

⁴⁹⁶ This provision of the *Corporations Act 2001* (Cth) provides for both public and proprietary companies. However, section 191(1) will not apply to a proprietary company with only one director. *Corporations Act 2001* (Cth) s 191(5).

⁴⁹⁷ *Corporations Act 2001* (Cth) s 191(1A).

⁴⁹⁸ A company's constitution may outline procedures when the event of a conflict arises for a director. Yet section 193 of the *Corporations Act 2001* (Cth) provides that in addition to the company's constitution the key provision of section 191(1) has effect to restrict a director from having material interest in a matter or holding an office involving duties or interest that conflict with their duties or interests as a director. A company's constitution in this regard must satisfy section 191 and not be in derogation of it. *Centofanti v Eekimitor Pty Ltd* (1995) 65 SASR 31.

⁴⁹⁹ *Corporations Act 2001* (Cth).

⁵⁰⁰ Harold Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 15th ed, 2013) 555-556.

⁵⁰¹ *McGellin v Mount King Mining NL* (SC(WA) (Murray J) CIV 1268/1997, 7 April 1998, unreported, BC9801129).

Further, section 191(1) refers to an indirect or direct interest.⁵⁰² A direct interest is self-explanatory, but an indirect interest often involves a third party. For instance, an indirect interest is when a director's relative holds an interest and, therefore, would benefit from a matter before the company's board. In this instance, it would be necessary to determine if there is a material personal interest.⁵⁰³

There is a list of exceptions under section 191(2), which does not require a director to provide disclosure or notice of an interest.⁵⁰⁴ From this list, only one feature is focused on, as pointed out, some of the incorporated association's legislation has adopted a similar exception for a committee members. Subsequently, a director does not have to give notice to disclose an interest if the interest arises because the director is a member of the company held in common with other members of the company.⁵⁰⁵

Finally, the procedure on how a director's interest is disclosed to the board is set out in section 191(3).⁵⁰⁶ This provision stipulates that a director must, in their notice to the board, outline sufficient details of the nature of the interest, the extent of the interest, and the relation of the interest to the company's affairs.⁵⁰⁷ The notice of disclosure must be given to the board as soon as practicable after the director becomes aware of the interest. Accordingly, the notice must be detailed in the company's minutes.

For a company, section 194 is a replaceable rule.⁵⁰⁸ Section 194 states that if a director of a proprietary company has a material personal interest that relates to the affairs of the company, and the director discloses the nature and the extent of the interest in relation to the affairs of the company at a director's meeting then it is in accordance with section 191.⁵⁰⁹ Where a director's interest does not need to be disclosed under section 191, that director can vote on matters relating to the interest and the interested transactions.⁵¹⁰ The vote may proceed and the director can retain

⁵⁰² *Corporations Act 2001* (Cth).

⁵⁰³ Harold Ford, Robert Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (Butterworths, 15th ed, 2013) 556.

⁵⁰⁴ *Corporations Act 2001* (Cth).

⁵⁰⁵ *Corporations Act 2001* (Cth) s 191(2)(a)(i).

⁵⁰⁶ *Corporations Act 2001* (Cth).

⁵⁰⁷ *Camelot Resources Ltd v McDonald* (1994) 14 ASCR 437.

⁵⁰⁸ *Corporations Act 2001* (Cth).

⁵⁰⁹ *Corporations Act 2001* (Cth).

⁵¹⁰ *Corporations Act 2001* (Cth).

the benefit from the transaction providing the transaction was entered into before the disclosure was made. Further, the company cannot avoid the transaction because the interest exists.

The provisions in Victoria, South Australia, Western Australia, Australian Capital Territory and Northern Territory deal with the disclosure of an officer's personal interest. Section 31(1) of the Northern Territory's *Associations Act 2003* states that a member of a committee who has a direct or indirect pecuniary interest in a contract or proposed contract with the association, must disclose the nature and the extent of the interest to the committee. The committee member must disclose this interest as soon as the member becomes aware and, further, the interests must be disclosed at the association's Annual General Meeting.⁵¹¹ This Northern Territory provision is clear as to how and when a committee member is required to disclose a pecuniary interest. The jurisdictions of Victoria, Australian Capital Territory, South Australia and Western Australia have the same wording in their disclosure provisions.⁵¹²

These state provisions are constructed differently from that of the *Corporations Act*.⁵¹³ The requirement of disclosure for incorporated associations only occurs if there is a direct or indirect pecuniary interest for a contract or a proposed contract; whereas, for a company director, there needs to be a material personal interest in a matter relating to the affairs of the company that could affect the board's deliberation. Circumstances where company directors must disclose their interests are wider than those for committee members. For instance, a company director may be required to disclose an interest relating to a transaction or in holding a specific position within another company; whereas, for a committee member, the requirement for disclosure only needs to be a mere interest, and it need only be disclosed to the management committee. Disclosure provisions for incorporated associations are restrictive, and this raises concerns that incorporated associations' legislation does not actively encourage sophisticated transparency in disclosing information.

Parallel to section 191(2) of the *Corporations Act 2001* (Cth), incorporated associations in Victoria, Western Australia, South Australia, and the Northern Territory have provisions where management committee members do not have to disclose their interests. Unlike section 191(2),

⁵¹¹ *Associations Act 2003* (NT) s 39(1)(a)-(b).

⁵¹² *Associations Incorporation Act 1981* (Vic) s 29B(1)-(2); *Associations Incorporation Reform Act 2012* (Vic) s 80; *Associations Incorporation Act 1985* (SA) s 31(1); *Associations Incorporation Act 1991* (ACT) s 65(1); *Associations Incorporation Act 1987* (WA) s 21.

⁵¹³ *Corporations Act 2001* (Cth) s 191.

the exceptions for incorporated associations are fewer and more obscure than for corporations. Specifically, committee members in the Northern Territory, Western Australia, South Australia and Victoria are not required to disclose their interest to the association if:

- a. they are employees of the association; or
- b. a member of a class of members for whose benefit the association is established; or
- c. the committee member's pecuniary interest is in common with all or a substantial proportion of the members of the association.⁵¹⁴

Incorporated associations' statutes provide that committee members with an interest in a contract or proposed contract are not permitted to vote or take part in the decision. However, an interested committee member can be present and take part in the committee's deliberations.⁵¹⁵ The obvious concern here is that the legislation allows for a committee member to wield his or her influence and power over other members to vote for in a manner that will benefit his or her interest.⁵¹⁶ However, in Western Australia and Victoria, there are stricter provisions compared to the other jurisdictions. An interested committee member in both of the jurisdictions are forbidden to take part in any deliberations or decisions of the committee,⁵¹⁷ but the legislation in Western Australia is silent in regards to allowing a committee member to vote on a decision in relation to an interested contract.⁵¹⁸ It can be said that a committee member participating in the deliberations undermines the aims of a disclosure regime.

Additionally, the timing and recording of a disclosed interest by committee members appears to be consistent across the jurisdictions that have disclosure provisions. These provisions require an interested committee member to disclose the nature and extent of his or her interest to the

⁵¹⁴ *Associations Act 2003* (NT) s 31(2); *Associations Incorporation Act 1981* (Vic) s 29B(2); *Associations Incorporation Reform Act 2012* (Vic) ss 80(3)-(4), 81(2); *Associations Incorporation Act 1985* (SA) s 31(2); *Associations Incorporation Act 1987* (WA) s 21(2). The Australian Capital Territory disclosure provision applies to committee members, but only if they are also employees of the association. *Associations Incorporation Act 1991* (ACT) s 65(3).

⁵¹⁵ *Associations Act 2003* (NT) s 32; ; *Associations Incorporation Act 1991* (ACT) s 65(2); *Associations Incorporation Act 2009* (NSW) s 31(5)-(6); *Associations Incorporation Act 1985* (SA) s 31.

⁵¹⁶ *Associations Incorporation Act 1987* (WA) s 21(1).

⁵¹⁷ *Associations Incorporation Act 1987* (WA) s 22; *Associations Incorporation Reform Act 2012* (Vic) s 81(1).

⁵¹⁸ *Associations Incorporation Act 1987* (WA) s 22. Section 81(1)(b) prohibits a committee member within a Victorian incorporated association to vote in a matter being considered by the committee where the committee member has a material personal interest. *Associations Incorporation Reform Act 2012* (Vic). See also *Associations Incorporation Reform Regulations 2012* (Vic) sch 4. Model Rule 65(2)(b).

management committee as soon as they have become aware of the interest.⁵¹⁹ Further, most of these jurisdictions (apart from Victoria) require the interested committee member to disclose their interests at the next annual general meeting of the association.⁵²⁰ The provision relating to recording an interest by a management committee member exists only in Victoria, Western Australia and the Northern Territory, where the interest of a committee member must be recorded in the minutes of the management committee.⁵²¹ Transparency or disclosure under these provisions takes a ‘bare foot’ approach to disclosure. Disclosure at an association’s annual general meeting may transpire months after an interest has become a conflict, and only then would the wider membership of the association become aware of the interest. This statutory regime does very little to encourage transparency or sharing of information, and this creates the risk of an ill-informed membership base and a perception of a tainted management committee.

New South Wales and Queensland’s disclosure regime is widely different from the other jurisdictions. Section 31 of New South Wales’ associations legislation provides that if a committee member has a direct or indirect interest in a matter being considered, or about to be considered, and the interest appears to raise conflict with the proper performance of the committee member’s duties, then the committee member must disclose the nature of the interest at a committee meeting.⁵²² This provision brings clarity to the duty of disclosing an interest and neatly folds in the duty to avoid a conflict, which is absent from the other jurisdictions. Unlike the other jurisdictions, the disclosure of an interest in New South Wales is broader in all matters, like transactions, agreements and other things, and not only contracts or proposed contracts.⁵²³ This provision encourages timely and efficient disclosure of a direct or indirect interest being considered, or about to be considered, by a management committee.

Pursuant to section 31(6), the committee must determine for itself whether the interested member can be present during the committee’s deliberation, or allow the interested member to

⁵¹⁹ *Associations Incorporation Act 1987* (WA) s 21(1); *Associations Incorporation Act 1985* (SA) s 31(1)(a); *Associations Incorporation Act 1981* (Vic) s 29B(1)(a); *Associations Incorporation Reform Act 2012* (Vic) s 80(1); *Associations Act 2003* (NT) s 32(1)(a).

⁵²⁰ *Associations Incorporation Act 1985* (SA) s 21(1)(b); *Associations Act 2003* (NT) s 31(1)(b).

⁵²¹ *Associations Incorporation Act 1987* (WA) s 21(4); *Associations (Model Constitution) Regulations 2004* (NT) reg 43; *Associations Incorporation Reform Act 2012* (Vic) s 80(6).

⁵²² *Incorporated Associations Act 2009* (NSW).

⁵²³ This interpretation of ‘matters’ lends itself from section 191(1) of *the Corporations Act 2001* (Cth).

take part in the committee's determination/decision regarding the relevant matter.⁵²⁴ However, before the management can agree to allow the interested member to vote or be present during deliberations, the interested member must give sufficient disclosure of the nature of the interest.⁵²⁵ This would see that a real discussion with the management committee would revolve around whether or not the interested party's decision would infringe upon his or her proper performance of their duties.

Furthermore, New South Wales is more astute in recording a member's interest. The legislation states that the committee must keep a book for that very purpose and must record all particulars of the disclosure.⁵²⁶ This book must be open at all reasonable hours for any member of the association to inspect; the book must be kept at the same address as the register of committee members, and must be open to all members to inspect the book that they know exists.⁵²⁷ New South Wales' disclosure provisions may be considered as exemplary for incorporated associations, and other jurisdictions should take note.

Queensland's provision regarding disclosure of an interest could, out of all the jurisdictions, be judged as sub-standard. Regulation 23(8) provides that a member of a management committee must not vote on a question about a contract or proposed contract if the member has an interest in the contract or proposed contract – and, if the member does vote, the vote cannot be counted.⁵²⁸ However, this provision is silent on whether a member with an interest is permitted to be present during deliberations.

Further, unlike other jurisdictions, Queensland's provision does not outline any procedural requirements to guide an interested officer to disclose the nature and the extent of his or her interest. Without a procedural requirement as to when or where a interest is to be disclosed, it would be tempting for a committee member not to disclose an interest, especially when that person may benefit indirectly from this undisclosed interest – the provision implies disclosure for a *direct* interest, which is very narrow.

⁵²⁴ *Associations Incorporation Act 2009* (NSW).

⁵²⁵ *Associations Incorporation Act 2009* (NSW) s 31(2).

⁵²⁶ *Associations Incorporation Act 2009* (NSW) s 32(3).

⁵²⁷ *Associations Incorporation Act 2009* (NSW) s 32(3),(4).

⁵²⁸ *Associations Incorporation Regulations 1999* (Qld).

Another point of concern is that if the interested officer does not abstain from the vote, how would this affect the validity of the contract? Unlike the *Corporations Act 2001* (Cth) and associations in other jurisdictions, Queensland's regulation does not express whether or not a contravention of the regulation would affect the validity of the contract. This conflict rule is contained in all associations' model rules. The lack of a disclosure requirement by the association's rules would inevitably lead to situations where an interested member may have a court render the contract unenforceable.⁵²⁹

Moreover, Queensland's provision for disclosure is contained within the subordinate legislation. This, unfortunately, does not provide any Queensland incorporated association with any legal duties that regulates the behaviour of a committee member under the *Associations Incorporation Act 1981* (Qld).⁵³⁰ The construction of the provision at its core does not deal adequately with transparency for members – it is a poor mechanism that does not afford a management committee the opportunity for a discussion of the issue.

Despite the known shortcomings of the *Corporations Act 2001* (Cth), it does provide a solid framework for directors' duties compared with the associations legislation. Table 6 succinctly shows the statutory legal duties for committee members across all jurisdictions are deficient and lag behind the *Corporations Act*.⁵³¹ However, the jurisdictions of South Australia, Northern Territory, New South Wales and Victoria can be seen to have made improvements with legal duties and obligations for an officer of a management committee.

Table 6 – Statutory duties of an incorporated association compared to a company⁵³²

Duty	SA	VIC	ACT	NSW	QLD	NT	WA	TAS	Company
Care, skill and diligence	✓	✓							✓
Proper use of position and information	✓	✓		✓		✓			✓
Pay debts	✓			✓		✓			✓
Reliance	✓	✓							✓

⁵²⁹ *Woolworths Ltd v Kelly* (1991) 22 NSWLR 189.

⁵³⁰ Section 87 imposes a duty on the association's secretary to register the association's interest in land. *Associations Incorporation Act 1981* (Qld).

⁵³¹ 2001 (Cth).

⁵³² Table 6 is adopted from the modified from an article by Charles Parkinson entitled 'Duties of Committee Members under the Associations Incorporation Acts' (2004) 30(1) *Monash University Law Review* 75.

Delegation						✓			✓
Disclosure of material interest		✓		✓		✓	✓		✓
Good faith		✓							✓
Proper purpose		✓							✓

5.4 Filling the Gaps in the Statutory Framework

There is a well-established body of common law and statutory duties that prohibit company directors from abusing their powers and, moreover, their position. For committee members, it is difficult to pinpoint a body of case law that applies specifically to not-for-profit associations. There have been encouraging developments in Victoria, South Australia and the Northern Territory to impose a positive statutory duties on committee members; however, for incorporated associations operating in jurisdictions without these statutory duty provisions, are there any rules that governs a committee member's conduct? The judgment of Owen J in the matter *Haselhurst v Wright* is examined to answer this question.⁵³³

Owen J was asked to grant an injunction on the grounds that the directors of a building society breached their fiduciary and common law duties.⁵³⁴ Before there could be a decision regarding the injunction, Owen J needed to look at a preliminary legal issue: if there was a breach, it first must be established whether a duty existed. Investigating whether or not there were legal duties owed by the building society's officers, Owen J examined the building society's governing legislation. Similar to incorporated associations, building societies have their own special legislation and are not touched by the corporations' law, and the building societies' legislation offered no assistance.⁵³⁵ Owen J simply noted that the duties owed by the building society's officers 'are to be found in the common law'. However, Owen J's statement is problematic on two grounds. First, there is no precedent that applies or develops common law duties for the management committee of an incorporated association.⁵³⁶ Secondly, Owen J does

⁵³³ (1991) 4 ACSR 527.

⁵³⁴ *Haselhurst v Wright* (1991) 4 ACSR 527 [35].

⁵³⁵ Section 1A of the *Associations Incorporation Act 1981* (Qld) expressly states that incorporated associations registered in Queensland are excluded from section 5F of the *Corporations Act 2001* (Cth). Other state and territory legislation have similar provisions in their associations' legislation. However, if an incorporated entity is limited by guarantee, then the *Corporations Act 2001* (Cth) will apply.

⁵³⁶ Johnson J in the decision of *Lai v Tiao (No 2)* [2009] WASC 22, 84 acknowledged that there is no authority that establishes an officer of incorporated associations owes common law duties.

not advance his statement by failing to recognise or pinpoint a substantive common law duty with which an officer of the building society is obliged to comply. The application of common law duties to officers of a management committee has shown to be improbable due to the leading decision of *Cameron v Hogan*.⁵³⁷

Cameron v Hogan established a long-standing policy that the courts refrain from interfering with the internal management and affairs of a voluntary association.⁵³⁸ This negative and long-standing policy has allowed the courts to regard many actions involving voluntary associations as non-justiciable.⁵³⁹ However, the courts in more recent times have shown some willingness to intervene, but only where an association has infringed the rules of natural justice and a member's economic interests, livelihood or reputation.⁵⁴⁰ Despite the courts slowly moving away from the strict policy position of *Cameron v Hogan*, would the courts go further and impose general law duties and obligations upon an officer of a management committee?⁵⁴¹ Most likely not – the courts have shown further unease to speak with an authoritative voice on matters involving voluntary associations, and where it seems convenient, the courts will resort to the policy of *Cameron v Hogan* to dismiss a claim.⁵⁴² Incremental advances by the courts may, in the future, reach a point where the judiciary will no longer consider issues involving voluntary associations as novel or insignificant, and the courts maybe more reticent in developing the common law duties specifically for voluntary associations.⁵⁴³ Returning again to Owen's J judgment, he held

⁵³⁷ (1934) 51 CLR 358.

⁵³⁸ (1934) 51 CLR 358. The reasons behind the High Court's policy of non-intervention are: rooted in nineteenth century view of the limits of judicial intervention; a respect for the association's privacy; and a fear that trivial and vexatious disputes will be encouraged which subsequently will open the 'floodgates' to litigation. John Forbes, *Judicial Review of Political Parties* (Research Paper No 21, Parliamentary Library, Parliament of Australia, 1995-1996) 3.

⁵³⁹ See *Carberry v Drice as Representative of Brisbane Junior Rugby Union* [2011] QSC 16; *Islamic Council of South Australia Inc v Australian Federation of Islamic Councils Inc* [2009] NSWSC 211; *Metropolitan Petar v Mitreski* [2003] NSWSC 1007; *Skelton v Australian Rugby Union Ltd* [2003] QSC 193; *Rush v WA Amateur Football Club League (Inc)* [2001] WASC 154; *Clarke v ALP (SA Branch)* [1999] SASC 415; *Plenty v Seventh Day Adventist Church of Port Pirie* (1986) 43 SASR 121; *Heale v Philips* [1959] QdR 489; *Abbott v National Coursing Association of South Australia* [1941] SASR 140.

⁵⁴⁰ See *Buckley v Tutty* (1971) 125 CLR 353; *Nurses Memorial Centre of South Australia v Beaumont* (1987) 44 SASR 455; *Carter v NSW Netball Association* [2004] NSWSC 737; *Dixon v Australian Society of Accountants* (1989) 87 ACTR 1.

⁵⁴¹ (1934) 51 CLR 358.

⁵⁴² (1934) 51 CLR 358. *Carberry v Drice as Representative of Brisbane Junior Rugby Union* [2011] QSC 16; *Islamic Council of South Australia Inc v Australian Federation of Islamic Councils Inc* [2009] NSWSC 211. Chapter Seven of this thesis analyses a range of legal duties for not-for-profit organisations in the United Kingdom.

⁵⁴³ The increased activity by parliament legislating regarding not-for-profit organisations may subsequently result in the courts' role to interpreting and giving effect to what parliament has legislated. Chapters Eight and Nine of this thesis analyses the federal government's legislative intentions for the not-for-profit sector and its organisations.

that fiduciary duties were owed by the society's directors to the body corporate, and the society's directors are to act in the society's best interest (as a whole) and to avoid being motivated by self-interest.⁵⁴⁴

5.5 Fiduciary Duties and Obligations

5.5.1 *Is an Officer of a Management Committee a Fiduciary?*

The ruling in *Haselhurst v Wright* is confined to a building society, and Owen J does not elaborate his finding as to why these specific directors are fiduciaries.⁵⁴⁵ This shortfall in this decision makes it difficult to conclude with any certainty as to whether officers of an incorporated association are also fiduciaries. Yet, the important aspect from Owen's J comment is that fiduciary duties are 'owed to the body corporate'.⁵⁴⁶ As it is known an incorporated association is a body corporate with perpetual succession and, for that reason, it is sound to conclude that under Owen's J finding this could be applied to an officer of a management committee and, therefore, conclude an officer of a management committee are fiduciaries and owe fiduciary duties to its association.⁵⁴⁷

5.5.2 *The Fiduciary Doctrine*

There are a number of established legal relationships that gives rise to fiduciary obligations and duties. These well-known, established categories are: trustee and beneficiary; principle and agent; employee and employer; solicitor and client; and director and company and partners.⁵⁴⁸ While these fiduciary categories are not closed, the task still remains difficult to identify a fiduciary in novel relationships due to the judiciary not establishing a strict formula to identify a fiduciary.⁵⁴⁹

⁵⁴⁴ *Haselhurst v Wright* (1991) 4 ACSR 527 [40],[45].

⁵⁴⁵ (1991) 4 ACSR 527.

⁵⁴⁶ (1991) 4 ACSR 527.

⁵⁴⁷ The respective state legislative provisions which confirms an incorporated association (upon registration) to be a body corporate are: *Associations Incorporation Act 1981* (Qld) s 21; *Associations Incorporation Act 2009* (NSW) s 8; *Associations Incorporation Act 1991* (ACT) s 22; *Associations Incorporation Act 1981* (Vic) s 38(2); *Associations Incorporation Act 1964* (Tas) s 11(1); *Associations Incorporation Act 1985* (SA) s 20(3); *Associations Incorporation Act 1987* (WA) s 10(a); *Associations Act 2003* (NT) s 11(a).

⁵⁴⁸ Paul Latimer, *Australian Business Law* (CCH, 30th ed, 2011) 744; P Finn, 'The Fiduciary Principle' in TG Youdan (ed), *Equity, Fiduciaries and Trusts* (1989) 1, 33–41.

⁵⁴⁹ *Virginia Surety Company Inc & Anor v Dumbrell & Ors* [2011] VSC 602; Denis Ong, *Trusts Law in Australia* (Federation Press, 3rd ed., 2007) 540. Attesting to the slow development of the fiduciary principle is Mason J who remarks that 'the fiduciary relationship is a concept in search of a principle'. Sir Anthony Mason, 'Themes and

Outside the established category of a charitable trustee and beneficiary, the task of identifying a fiduciary relationship existing in the not-for-profit context is not as obvious. Both Seivers and Latimer state that a committee member of an unincorporated association *may* (my emphasis) have fiduciary obligations to members.⁵⁵⁰ This *carte blanche* statement, in the same way as Owen J, is made without explanation or justification. While on the surface it may seem obvious, however, it is not easy to denote that a committee member is a fiduciary. The fundamental question always asked when trying to establish a fiduciary relationship is: what is a fiduciary? This question too cannot always be simply answered.

5.5.3 What is a Fiduciary?

The general approach taken by the Australian courts in identifying a fiduciary is founded in a legal relationship⁵⁵¹ that is outside the parties' legal obligations in contract and torts.⁵⁵² The parties' legal relationship will be of a particular nature, which exhibits trust and confidence, where the fiduciary will undertake to, or agree, to act for or on behalf of another person.⁵⁵³ Acting on behalf of another provides the fiduciary with discretion to exercise power that will affect the interest of somebody who, within this relationship, is in a position of disadvantage and vulnerability.⁵⁵⁴ This description of a fiduciary relationship outlines particular characteristics that can easily be applied to an officer of an unincorporated and incorporated association. The application of these features can be seen when an individual takes on the role of an officer of the management committee: they undertake to act for the interests of the association. Further, by acting on behalf of the association, an officer has the power and the discretion (by virtue of his or her position) to make decisions that will affect the association and its members. Further, an officer is trusted to make decisions that will benefit the association and its members. However,

Prospects' in PD Finn (ed.), *Essays in Equity* (1985) 246. Adding to the tempered vagueness of fiduciary is expressed by Jacobson J that is, 'the term 'fiduciary relationship' defies definition'. *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Limited (ACN 113 114 832) (No 4)* [2007] FCA 963 at 270.

⁵⁵⁰ A. S. Seivers, *Associations and Clubs Laws in Australia and New Zealand* (Federation Press, 3rd ed, 2010) 17; Paul Latimer, *Australian Business Law* (CCH, 30th ed, 2011) 744.

⁵⁵¹ See *Hospital Products Limited v United States Surgical Corporation* (1984) 156 CLR 41; *Maguire v Makaronis* (1997) 188 CLR 449; *Estate Realities Ltd v Wignall* [1991] 3 NZLR 482.

⁵⁵² Peter Radan and Cameron Stewart, *Principles of Australian Equity and Trusts* (LexisNexis Butterworths, 2010) 181.

⁵⁵³ *Hospital Products Limited v United States Surgical Corporation* (1984) 156 CLR 41, 96 (Mason J).

⁵⁵⁴ *Hospital Products Limited v United States Surgical Corporation* (1984) 156 CLR 41, 96, 142 (Mason and Dawson JJ).

this arrangement places members in vulnerable position where an officer can abuse the power and position.⁵⁵⁵ Hence, it is very easy to see why Sievers and Latimer concluded that officers of unincorporated and incorporated associations are fiduciaries and, therefore, owe fiduciary duties. However, doubt remains over whether the last characteristic of vulnerability is truly present in the relationship between an officer and the association's members.

There are possibilities where members of the association and its property are vulnerable to abuse by an officer of the management committee. Giving rise to this possibility is the statutory power of control and power vested in the management committee to operate and conduct the association's business.⁵⁵⁶ This unqualified power allows an/the officer/s of a management committee to make decisions about the association's affairs and property without the need for the membership base to be involved or consulted in the decision-making process.⁵⁵⁷ However, to counterbalance this exclusive power, the association's rules provide members with voting rights.⁵⁵⁸ Each member of an association has one vote, and the rules provide that a majority of members present can decide on matters by way of a resolution at a general meeting.⁵⁵⁹ This facilitates a democratic method of decision-making that ensures the administration of the association is being conducted in a proper manner.

⁵⁵⁵ The feature of trust is impulsive due to the notion that not-for-profit organisations are more trustworthy than for-profits as a consequence of information asymmetry, contract failure, and the perception that an officer is wholesome and selfless when perusing and undertaking the association's unadulterated and altruistic purposes. D. Young, 'Alternative Models of Government-Nonprofit Sector Relations: Theoretical and International Perspectives' (2000) 29 *Nonprofit and Voluntary Sector Quarterly* 149, 154; Lester Salamon, 'Putting the Civil Society Sector on the Economic Map of the World' (2010) 81(2) *Annals of Public and Cooperative Economics* 167, 168-169. Refer to Chapter Two of this thesis for a further explanation of information asymmetries, contract failure, and the trustworthy theory.

⁵⁵⁶ *Associations Incorporation Act 1981* (Qld) s 60(1).

⁵⁵⁷ For example, in Queensland the management committee must decide whether there is a need for the association to take out public liability insurance and the amount of public liability insurance. This decision by the management committee in regards to not taking out public liability insurance is to be reported at the association's annual general meetings. *Associations Incorporation and Other Legislation Amendment Act 2007* (Qld) ss 70, 70A.

⁵⁵⁸ *Associations Incorporation Regulations 1999* reg 38(2); *Associations Incorporation Regulations 2010* (NSW) reg 22(2); *Associations Incorporation Regulations 1991* (ACT) reg 20(2); *Associations Incorporation Act 1981* (Vic) s 29(5); *Associations Incorporation Regulations 2009* (Vic) reg 16(1); *Associations Incorporation (Model Rules) Regulations 2007* (Tas) reg 18(1); *Associations Incorporation Act 1988* (WA) 1987 s 24; *Associations (Model Constitution) Regulations 2004* (NT) reg 40(1). There is no provision within the *Associations Incorporation Act 1985* (SA) nor its accompany regulations which expressly states that a member has one vote. However, the publication entitled *An Example of Rules for Incorporated Associations* produced by the Government of South Australia, Consumers and Business Services states that a member of an incorporated association has only one vote. South Australia Government, *An Example of Rules for Incorporated Associations* (undated) <http://www.ocba.sa.gov.au/assets/files/02_association_rules.pdf> 12.

⁵⁵⁹ *Association Incorporation Regulations 1999* (Qld) sch 4, reg 38.

However, where members do not have voting rights, the management of the organisation is centralised amongst an exclusive few individuals, and this will create a private sphere. Within this private sphere, all the decisions regarding the management of the association will be made. How decisions are made and how individuals conduct themselves within this sanctum is out of view without the need to be answerable to the membership base.⁵⁶⁰ Acting independently to the rest of the association, this private sphere will become insular, allowing an individual to act *bona fide* in self-interest. The management of the association falls upon the shoulders of a few, and these few individuals will become highly involved in the association and possess the necessary knowledge on how to manage it. Members will come to trust and blindly accept any information provided by these individuals. This will allow the dominant personalities to orchestrate the numbers amongst the membership base to support their agenda – this can occur regardless of whether members have voting rights or not.⁵⁶¹ The private sphere that emerges in this instance is because these few individuals have a monopoly in the management of the organisation. Worst of all, the structure of associations allows such individuals to self-regulate, which will permit any acts of self-interest or other misdeeds to be hidden from the membership base and, consequently, members would be in a vulnerable situation. However, the finding of a fiduciary relationship in a novel situation remains an impossible task, despite the presence of vulnerability.⁵⁶²

The courts are highly reluctant to impose a higher standard of conduct prescribed under equity to those in a ‘relative equal position’.⁵⁶³ Further, reluctance by the court to impose fiduciary obligations will bring about uncertainty in a commercial context.⁵⁶⁴ While the relationship between an officer and member is not commercial in nature the relationship, it is, however, contractual; it is this aspect of the parties’ relationship that the courts would focus upon.⁵⁶⁵

⁵⁶⁰ Kim Weinert, ‘Is there a Perfect Environment for a Villian and Villaniness to Survive?’ in Rachel Franks and Susan E. Meindi (eds), *The Real and Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 53.

⁵⁶¹ *McClelland v Burning Palms Surf Lifesaving Club* [2002] NSWCA 470.

⁵⁶² *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41.

⁵⁶³ Anthony Mason, ‘The Place of Equity and Equitable Remedies in the Contemporary Common Law World’ (1994) 110 *Law Quarterly Review* 238, 238.

⁵⁶⁴ Steven White, ‘Commercial Relationships and the Burgeoning Fiduciary Principle’ (2000) 9(1) *Griffith Law Review* 98, 99. Dawson J expressed that confusion and uncertainty will occur in commercial dealings if the fiduciary principle was imposed. *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 [494].

⁵⁶⁵ The rules of an incorporated association operate as a contract between the association and its members. *McClelland v Burning Palms Surf Life Saving Club* [2002] NSWSC 470.

The finding that an officer of an organisation is a fiduciary seems unlikely. Identifying the core of an officer's relationship to another member and to the association itself is rooted in contract and, moreover, this contract places each officer and member on an equal footing. The courts would prefer to elicit an officer's and a member's obligations from contract and not draw upon stricter equity principles that may alter the operation of the contract.⁵⁶⁶ Although courts seem impervious to a plea of a fiduciary relationship, they will, however, afford the opportunity for a party to argue for a finding of a fiduciary relationship.⁵⁶⁷

The opportunity to argue that an officer of a not-for-profit organisation was a fiduciary happened in the Canadian case of *London Humane Society (Re)*.⁵⁶⁸ Here it was found that an officer of a not-for-profit organisation is a fiduciary due to their discretion over the organisation's property – the interest remained vested in the organisation, not the members.⁵⁶⁹ Therefore, an officer of a not-for-profit organisation is in a fiduciary relationship with organisation itself,⁵⁷⁰ and the public.⁵⁷¹ These findings by the Canadian courts are not surprising. Compared with Australia, the development of fiduciary law in Canada has been progressive, and the fiduciary doctrine has been widened to include relationships where there are non-economic interests.⁵⁷² Furthermore, the analysis of a fiduciary relationship is prescriptive, which subsequently has created a 'catch-all' situation, unlike Australia's approach, which is prospective.⁵⁷³ However, it remains to be seen whether the Australian judiciary would be amenable to view an officer of an incorporated association as a fiduciary.

The law confers some nominal statutory duties, but no rules to govern the conduct of an officer who has control of an association's funds and property. This is unacceptable and, therefore, a different view of an officer of a voluntary association is needed to find and recognise

⁵⁶⁶ *Hospital Products Ltd V United States Surgical Corp* (1984) 156 CLR 41[97] (Mason J).

⁵⁶⁷ *Virginia Surety Company Inc & Anor v Dumbrell & Ors* [2011] VSC 602 [35].

⁵⁶⁸ (2010) ONSC 5775.

⁵⁶⁹ (2010) ONSC 5775.

⁵⁷⁰ *London Humane Society (Re)* (2010) ONSC 5775.

⁵⁷¹ The court found that the fiduciary relationship between an officer and the public is largely due to the public making donations to the organisation. *Pathak v Hindu Sabha* (2004) O.J No. 1981.

⁵⁷² *Frame v Smith* (1987) 42 DLR (4th) 81.

⁵⁷³ *Norberg v Wynrib* (1992) 92 DLR (4th) 449; Leonard Rotman, 'Fiduciary Doctrine: A Concept in Need of Understanding' (1996) 34(4) *Alberta Law Review* 821, 833.

some rules of obligations that are applicable to an officer of an association. This alternative view would be to see an officer as an ‘agent’ of the association.

5.5.4 *Principal Agent Relationship*

Viewing an officer as an agent the law would subject that person’s conduct to certain duties and obligations. The decision and policy of *Cameron v Hogan* has repeatedly been shown to be a barrier for the courts to adequately deal with grievances involving a not-for-profit organisation – as surprising as it may seem, *Cameron v Hogan* can be helpful in identifying an officer as an agent.⁵⁷⁴ The majority stated in *Cameron* that officers may be agents for the members of the association and, furthermore, stated that upon there being no doctrine of agency, an association’s members are joint principals who can hold an officer and the committee responsible.⁵⁷⁵

The incorporated association legislation offers some guidance in knowing whether an officer of a management committee is an agent; however, there remains inconsistency across most of the jurisdictions. Queensland is the only jurisdiction that expressly states every member of the management committee, and any manager appointed by the management committee, are deemed to be agents of the association.⁵⁷⁶ However, the remaining jurisdictions do not provide such clarity.

New South Wales’ incorporated association’s legislation notes that any people who hold themselves out to be an agent of the association can make the assumption that this person is duly appointed and has the authority to be an agent.⁵⁷⁷ This provision is a direct reflection of the indoor management rule found in section 129 of the *Corporations Act 2001* (Cth). Furthermore, section 126 of the *Corporations Act 2001* (Cth) the New South Wales’ Act states that an agent has an association’s expressed and implied authority to make, vary, ratify or discharge a contract on behalf of the association.⁵⁷⁸ These provisions in the New South Wales’ statute are wide, and

⁵⁷⁴ In more recent times, the lower courts have shown their preparedness to hear disputes regarding the members of an incorporated association. While these decisions found there to be a breach of natural justice, the courts did not find a member’s contractual interests and rights were infringed. See *Rose v Boxing NSW Inc* [2007] NSWSC 20 and *Goodwin v VVMC Club Australia (NSW Chapter)* [2008] NSWSC 154. Both of these judgments found that the association had inadequately dealt with a dispute with a member and ordered compensation.

⁵⁷⁵ *Cameron v Hogan* (1934) 51 CLR 358 (Rich, Dixon, Evatt and McTiernan JJ); *Kelly v National Society of Operative Printers* (1916) 113 L.T 1055.

⁵⁷⁶ *Associations Incorporation Act 1981* (Qld) s 60(2).

⁵⁷⁷ *Associations Incorporation Act 2009* (NSW) s 24(4).

⁵⁷⁸ *Associations Incorporation Act 2009* (NSW) s 21(1).

they do not specify how and who within the association can be appointed as an agent. The danger of these provisions is that any person purporting to be an agent may bind an association to a contract or transaction that the association may not know about, want, or is within the purpose of the association. These provisions strongly imply that an association's agent is entrusted to undertake dealings in good faith. While under the general law an unruly agent may be personally liable for their actions, the legislation does not provide any liability provisions for agents or individual purporting to be agents. However, the other states provide stricter provisions relating to an agent's conduct.

Respective legislation in the Australian Capital Territory, Western Australia, South Australia and Victoria states that an agent may execute documents and deeds under the association's common seal.⁵⁷⁹ These jurisdictions require an agent to be appointed in writing and the agent's authority continues only for a period specified in the instrument that confers the agent's authority – and, if no period is stated, revocation or termination of the agent's authority by way of notice.⁵⁸⁰ These provisions can be assessed to be applicable only to the association appointing a specific individual to undertake a one-off task, such as purchasing property. Nothing within these jurisdictions suggests a member or an officer of the management committee is automatically an agent. The jurisdictions of the Tasmania and the Northern Territory contain no provisions that allow for the appointment of an agent to act on the association's behalf.

These gaps in the legislation raise two queries. First, whether officers of a management committee are agents for the association in the jurisdictions of South and Western Australia, Victoria, Tasmania and the Northern Territory; and, secondly, whether is it probable that associations in Tasmania and the Northern Territory have the power to appoint an agent. The last relies on the legal instrument that provides an association with a juristic personality. This, subsequently, allows an association to have the legal capacity to exercise powers carry out the organisation's business, which endows an association the ability to enter into contracts.⁵⁸¹ This

⁵⁷⁹ *Associations Incorporation Act 1991* (ACT) s 55(2); *Associations Incorporation Act 1991* (SA) s 55(1); *Associations Incorporation Act 1981* (Vic) s 19(7); *Associations Incorporation Reform Act 2012* (Vic) s 39; *Associations Incorporation Act 1987* (WA) s 13(1)(f).

⁵⁸⁰ *Associations Incorporation Act 1991* (SA) s 55(2),(3); *Associations Incorporation Act 1981* (Vic) s 19(8); *Associations Incorporation Reform Act 2012* (Vic) s 39(3).

⁵⁸¹ *Associations Incorporation Act 1981* (Qld) s 25; *Associations Incorporation Act 2009* (NSW) ss 19, 21; *Associations Incorporation Act 1991* (ACT) s 42; *Associations Incorporation Act 1981* (Vic) s 19; *Associations*

juristic personality allows an association to appoint an agent by contract or in writing to act on behalf of the association. However, with regards to the first query (whether an officer is an agent in the remaining jurisdictions) remains unclear and, therefore, attention is turned to the general law.

The *Cameron v Hogan* decision provides a clear answer to the query – the majority stated that an officer may be an agent for the association and its members.⁵⁸² Their Honours failed to explain why an officer is an agent and, in the absence of any judicial reasoning, it maybe presumed that a finding of agency arises out of necessity to carry out transactions and the association’s activities – regardless of whether the association is incorporated or unincorporated.

Nevertheless, there is some difficulty determining whether an individual committee member of an unincorporated association is an agent due to the law not recognising this particular form as a juristic entity and, furthermore, any transaction or contract involving an unincorporated association needs to be in the officer’s own name.⁵⁸³ However, these concerns are overcome by the decision of *Kelly v National Society of Operative Printers*.⁵⁸⁴ Here, the majority found that an officer of an unincorporated body is an agent.⁵⁸⁵ An officer acting as an agent of either incorporated or unincorporated associations will not receive remuneration, nor will the agent be subject to an enforceable contract of agency. Therefore, in the absence of an enforceable contract, an officer would be found to be a gratuitous agent.⁵⁸⁶ Once an agency relationship has been established, it must be determined what is the agent’s authority.⁵⁸⁷

5.5.5 An Agent’s Authority

The scope of an agent’s authority is important when considering whether that agent has acted outside his or her authority and, consequently, would lose the right of indemnity for their actions.

Incorporation Act 1964 (Tas) s 20; *Associations Incorporation Act 1985* (SA) s 26; *Associations Incorporation Act 1987* (WA) ss 14, 20; *Associations Act 2003* (NT) pt 4.

⁵⁸² *Cameron v Hogan* (1934) 51 CLR 358 (Rich, Dixon, Evatt and McTiernan JJ).

⁵⁸³ *Freeman v McManus* [1958] VR 15; *Carlton Cricket and Football Social Club v Joseph* [1970] VR 487.

⁵⁸⁴ (1916) 113 L.T. 1005.

⁵⁸⁵ (1916) 113 L.T. 1005, 1058, 1062 (Swinfen Eady L.J, Phillimore L.J and Bankes L.J).

⁵⁸⁶ *Yasuda Fire & Marine Insurance Co of Europe Ltd v Orion Marine Insurance Underwriting Agency Ltd* [1995] 3 All ER 174, 185.

⁵⁸⁷ *Credit Lyonnais Bank Nederland NV v ECGD* [2001] 1 AC 486.

The types of authority are: (a) actual authority, implied and expressed; (b) ostensible authority; and (c) retrospective authority.⁵⁸⁸

The type of authority conferred upon an agent derives from the source that creates the agency and principle relationship. As already established, an officer of an incorporated association is an agent under the respective association legislation that provides an agent (officer) with actual authority. The agent being conferred with the authority to perform particular acts in the name of the association creates this actual authority. Furthermore, an officer's actual authority may be implied by the agent's conduct, the circumstances, or activities that are incidental to the association's activities.⁵⁸⁹ The rules governing an agent's apparent authority (regardless whether it is expressed or implied) the doctrine of *ultra vires* may be a consequence for an officer who has acted outside his or her authority.

The doctrine of *ultra vires* has been disposed of by the association legislation. Under the associations' statute, the *ultra vires* rule has been altered regarding the power of an officer to enter into a binding agreement with the association – it shall not be invalid where the association did not have the power or the capacity to do such an act or to execute the document.⁵⁹⁰ Where an association lacks the power to execute a transaction, the courts are willing to remedy this through the rules of constructive trust – especially where unincorporated associations are involved.⁵⁹¹ Despite the doctrine of *ultra vires* being set aside by statute, the conduct of an agent of an incorporated association will remain subject to the recognised general law duties of an agent.

5.5.6 Duties of an Agent

The principal and agent relationship gives rise to certain and onerous duties for an agent.⁵⁹² McCardie J in *Armstrong v Jackson* stated that these particular and onerous duties are due to the agent's position of confidentiality, and situations that can lend themselves to abuse or to be taken

⁵⁸⁸ Simon Fisher, *Agency Law* (Butterworths, 2000) 32-39.

⁵⁸⁹ *Verdi Club Inc v National Australia Bank* (1991) 104 FLR 344; Roderick Munday, *Agency Law and Principles* (Oxford University Press, 2010) 48-51.

⁵⁹⁰ *Associations Incorporation Act 1981* (Qld) s 26; *Associations Incorporation Act 2009* (NSW) s 20; *Associations Incorporation Act 1991* (ACT) s 56; *Associations Incorporation Act 1981* (Vic) s 17; *Associations Incorporation Reform Act 2012* (Vic) s 35; *Associations Incorporation Act 1985* (SA) s 27; *Associations Incorporation Act 1987* (WA) s 15. Constructive notice will not be discussed, as it is not in the scope of this thesis.

⁵⁹¹ *Worthing Rugby Football Club v Inland Revenue Commissioners* [1985] 1 WLR 409. Chapter Four of this thesis outlines the pragmatic difficulties of an unincorporated association due to its poor legal standing.

⁵⁹² *Armstrong v Jackson* [1917] 2 KB 822, 826 (McCardie J).

advantage of and, therefore, requires the agent's conduct to be of a high standard.⁵⁹³ The essence of McCardie's J judgement illustrates that there is a fiduciary dimension to the principal agent relationship and that strict equitable principles apply.⁵⁹⁴ Gibbs CJ and Mason J in *Hospital Products Ltd v United States Surgical Corp* also support this position by recognising that the principal agency relationship is a fiduciary relationship.⁵⁹⁵ Further, to the strict equitable obligations owed by an agent to the principle that arises from the special position of trust, there are also an agent's contractual duties.⁵⁹⁶

The respective incorporated association legislation allows an officer to operate as an agent of the association; however, neither the statute nor the association's rules provide an agent with any rules, duties or obligations specific to an agent.⁵⁹⁷ Therefore, it is plausible to find an officer as a gratuitous agent due to the absence of remuneration and an enforceable contract.⁵⁹⁸ Establishing that an officer is a gratuitous agent poses the question: does that officer owe the association the fiduciary duties of an agent or a lesser duty of care?⁵⁹⁹

Where an officer is a gratuitous agent (appointed by statute), it is reasonable for an association to rely and trust on that agent's skill and judgement. However, the members must also have confidence that an agent's performance will be carried out in accordance with the fiduciary duties of an agent.⁶⁰⁰ The fiduciary duties owed by an agent are as follows:

1. *no conflict rule* – officers must not be in conflict with the association and they should not take advantage if a conflict arises;⁶⁰¹
2. *no profit rule* – an officer must not receive a profit at the expense of the association;⁶⁰²

⁵⁹³ [1917] 2 KB 822, 826.

⁵⁹⁴ *Armstrong v Jackson* [1917] 2 KB 822, 825-826 (McCardie J).

⁵⁹⁵ (1984) 156 CLR 41 [68], [96] (Gibbs CJ and Mason J).

⁵⁹⁶ *Rothschild v Brookman* (1831) 5 Bli (NS) 165, 197; *O'Sullivan v Management Agency and Music Ltd* [1985] QB 428, 451; *Morris v CW Martin & Sons Ltd* [1996] 1 QB 716.

⁵⁹⁷ Many incorporated associations rely and operate on the efforts of volunteers who occupy positions on the management committee, and it would be a fair assessment that these volunteers generally would not have any knowledge or understanding of an agent's duties. Therefore, the respective incorporated associations legislation should outline these obligations.

⁵⁹⁸ An association's rules can be read to have the effect of a contract. *Islamic Council of South Australia Inc v Australian Federation of Islamic Council Inc* [2009] NSWSC 211; *Liddle v Central Australian Legal Aid Service Inc* [1999] NTSC 35.

⁵⁹⁹ *Chaudhry v Prabakhar* [1989] 1 WLR 29.

⁶⁰⁰ *Bristol & West BS v Mathew* [1998] Ch 1, 18 (Millett LJ).

⁶⁰¹ *Western Areas Exploration Pty Ltd v Streeter (No 3)* [2009] WASC 213, 48.

⁶⁰² *Cook v Deeks* [1916] 1 AC 554.

3. *duty of loyalty* – an officer must make all the relevant information available to the association;⁶⁰³ and
4. *duty of confidentiality* – any information obtained by the officer for the association must not be used by that officer for a private advantage.⁶⁰⁴

Conversely, the required level of care a gratuitous agent owes a principal is declared to be what might be reasonably expected in the circumstances and, furthermore, judged objectively.⁶⁰⁵ This means that an agent's actual degree of skill and experience, or the skill and experience that the agent has laid on themselves.⁶⁰⁶

The strictness of these fiduciary duties for officers raises the old argument that it would be unreasonable to expect volunteers to satisfy this high standard on the basis that individuals are acting out of prevailing social mores. The courts would give strong consideration to this argument, and would more than likely find that the lower common law duty applies. Where officers do not hold themselves out to have a special skill or knowledge, the court has held that, in the circumstances, a gratuitous agent will be held to the standard of care of a competent agent when carrying out the business of the association.⁶⁰⁷ The court held there are no grounds to exempt a gratuitous agent from a duty of care when they are entrusted to carry out a task.⁶⁰⁸ Hence, officers of incorporated and unincorporated associations acting as an agent for them can be a fiduciary – but it is more than likely a court will hold an agent to a minimal standard of care and not to strict fiduciary obligations.

5.6 Conclusion

There are some similarities between the roles and functions of a company director and an officer of a management committee. Both operate as a collective group of individuals who are in control of and manage their respective entity's property and carry out the operation and business. There is very little known about how a management committee carries out these functions. There is, of course, a desired presumption and expectation that a management committee of an association

⁶⁰³ *Breen v Williams* (1996) 186 CLR 71.

⁶⁰⁴ *Morison v Moat* (1851) 68 ER 492, 898.

⁶⁰⁵ *Chaudhry v Prabakhar* [1989] 1 WLR 29 (Stocker and Stuart-Smith LJ).

⁶⁰⁶ *Chaudhry v Prabakhar* [1989] 1 WLR 29.

⁶⁰⁷ *Norwest Refrigeration Services Pty Ltd v Bain Dawes (WA) Pty Ltd* (1984) 157 CLR 149, 168-70 (Brennan J).

⁶⁰⁸ *Norwest Refrigeration Services Pty Ltd v Bain Dawes (WA) Pty Ltd* (1984) 157 CLR 149, 169 (Brennan J).

manages in accordance with the association's altruistic mission. However, the altruistic mission can no longer be a shield to deflect the need for better accountability and transparency of not-for-profit organisations.

There are overwhelming social and economic reasons to justify the call for better transparency and accountability through a governance framework within not-for-profit organisations. Unfortunately, the law relating to incorporated associations does very little to encourage a management committee to achieve transparency and accountability, or to promote a governance framework that protects an association's property and controls risk. Legal duties and obligations are important mechanisms of organisational governance, and an examination of legal duties for incorporated associations reveals a number of shortcomings.

Chapter Five first analysed an officer's statutory duties across state and territory jurisdictions. This analysis illustrated that New South Wales, South Australia and the Northern Territory have more statutory duties compared to the other jurisdictions. Furthermore, these jurisdictions have made advances and improvements by introducing some statutory duties. Table 6 succinctly shows the statutory duties of committee members across all Australian jurisdictions, and demonstrates inconsistencies in statutory duties for officers of a management committee. Where there are significant gaps in the legislation, the general law is considered.

The general law has proved unhelpful in ascertaining whether an officer of a management committee is subject to common law duties. There are no common law duties due to the long-standing decision of *Cameron v Hogan*,⁶⁰⁹ which set the precedent that, in the absence of a proprietary right or interest in the property of the association, any issue regarding the internal management of a voluntary association is non-justiciable. Despite incremental advances by the courts to intervene in some matters involving the internal management of voluntary associations, the courts have, however, been reluctant to develop common law duties for officers of a voluntary association. Chapter Five shows that, in a number of cases, it has been held that an officer owes some general law duties. Where the common law has shown to be scant, the fiduciary law has been shown to be of some assistance.

⁶⁰⁹ (1934) 51 CLR 358.

However, for fiduciary duties to be owed, it must be established that an officer is a fiduciary and that an officer has a fiduciary relationship with the association. The established fiduciary categories do not include an officer of a management committee or a voluntary association.

The courts do not wish to hold an individual to stricter or a higher standard of conduct especially where the parties are in a relatively equal position by showing that an officer and a member of an association are in an equal position. With very few statutory, common law and fiduciary duties affecting the conduct of an officer an alternative view of the role of the officer is needed.

Identifying an officer as an agent will, in fact, subject that officer's conduct to strict fiduciary duties in particular circumstances. The circumstances in which an agent owes fiduciary duties were clearly stated by Lord Denning MR *Broadman v Phillips* [1965] Ch 992 at 1018-19 when he said:

... if an agent uses property, with which he has been entrusted by his principal, so as to make a profit for himself out of it, without his principal's consent, then he is accountable to his principal ... So, also, if he uses a position of authority, to which has been appointed by his principal, so as to gain money by means of it for himself, then also he is accountable to his principal for it ... Likewise with information or knowledge which he has been employed by his principal to collect or discover, or which he has otherwise acquired, for the use of the principal, then again if he turns it to his own use, so as to make a profit by means of it for himself, he is accountable ... for such information or knowledge is the property of his principal, just as much an invention is ...

Notwithstanding the negative impact of *Cameron v Hogan*,⁶¹⁰ it was stated by the majority (Rich, Evatt, and McTiernan, JJ) that an officer may be an agent, and members of an unincorporated association are joint principals. Furthermore, the English Court of Appeal decision of *Kelly v National Society of Operative Printers*, cited by the majority in *Cameron v Hogan*,⁶¹¹ found that an officer of an unincorporated association maybe an agent.⁶¹² The respective associations' legislation also gives some additional support to the concept that an officer is an agent of the

⁶¹⁰ (1934) 51 CLR 358.

⁶¹¹ (1934) 51 CLR 358, 373.

⁶¹² (1916) 113 L.T 1055, 1058, 1060, 1062.

association with actual authority. While the respective legislation does not identify the type of agent the common law would most likely view an officer to be a gratuitous agent when dealing with third parties. The standard of care for a gratuitous agent will take into account the agent's actual degree of skill, judgment and experience that they hold themselves out to have. Furthermore, the courts have shown little tolerance to exempt a gratuitous agent from liability and, therefore, in the circumstances, a gratuitous agent has been held to a minimal standard of care opposed to that expected of a competent agent. This, however, is reflective of torts law and not fiduciary principle as such.

PART III

Shaping Australia's Not-for-Profit Sector for the Future

CHAPTER 6: Future Movements within Our Not-for-Profit Sector

*... a community needs to nurture their not-for-profit sector, which in turn nurtures our nation.*⁶¹³

6.0 Introduction

Before 1999, the Australian parliament showed very little interest in understanding the needs of the not-for-profit sector. However, over the past decade, the federal government's interest in the not-for-profit sector has grown. Through the commissioning of a number of parliamentary inquiries and reports, the not-for-profit sector is earmarked for reform. This chapter will highlight the background that prompted the key reports from the Productivity Commission⁶¹⁴ and a Senate inquiry.⁶¹⁵ Both reports conceded that the current regulatory environment for all forms of not-for-profit organisations is not effective and recommended a number of key reforms. Chapter Six outlines the common themes of reform in the areas of regulation and governance that have emerged from these two reports.

6.1 Federal Parliamentary Inquiries and Governmental Reports

The federal parliament has commissioned a number of inquiries and reviews into the not-for-profit sector (see Table 7 for a chronology of the federal parliamentary inquiries and reports). The aim of each inquiry was not only to improve our policy makers' knowledge and understanding of the sector, but also to gather ideas on how to best reform our not-for-profit sector. The reform discussion and agenda initially focused on financial reporting and accountability but, over time, the discussion widened to include: fundraising; taxation; government partnerships; funding; contracting and tendering; regulation; and how best to measure the sector's outputs. No doubt all aspects of these discussions are important; however, this thesis will concentrate on the core

⁶¹³ 'Simon McKeon named Australian of the Year', ABC News (online) 26 January 2011
<<http://www.abc.net.au/news/starcs/2011/01/25/3121659.htm>>.

⁶¹⁴ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010).

⁶¹⁵ Senate Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) Chapter 2.

themes of governance being regulation and financial reporting from the Senate's Disclosure Inquiry and the Productivity Commission's report.

Table 7 – Chronology of recent federal parliamentary inquiries, reports, studies and reviews⁶¹⁶

Title	Committee/Department	Date
Inquiry Report: Inquiry into the Definition of Charities and Related Organisations	The Senate- Senate Standing Committee on Economics	June 2011
Discussion Paper: Financial Reporting by Unlisted Public Companies	The Treasury	June 2007
Inquiry Report: Inquiry into the Disclosure Regimes for Charities and Not-for-Profit Organisations	The Senate- Standing Committee on Economics	December 2008
Report to the Treasurer – Australia's Future Tax System	The Treasury	December 2009
Report: Tax Laws Amendment (Public Benefit Test) Bill 2010	The Senate- Economics Legislation Committee	September 2010
Report: Contribution of the Not-for-Profit Sector	Productivity Commission	January 2010
Consultation Report: National Compact between the Australian Government and Third Sector	Australian Government	February 2010
Consultation Paper: Scoping Study for a National Not-for-Profit Regulator	The Treasury	January 2011

6.2 Disclosure Regime for Charities and Not-for-Profit Inquiry

6.2.1 Background to the Disclosure Inquiry

Seven years after the 2001 inquiry into the definition of charity, the Howard government took no action to reform the not-for-profit sector,⁶¹⁷ despite the federal government agreeing 'in principle' to implement the twenty-seven recommendations.⁶¹⁸ This inaction by the government prompted then-senators Allison and Murray to initiate a motion for another inquiry into the sector. Senator Allison's motion highlighted the need for a second inquiry based on the findings from CHOICE's on-line article relating to charities.⁶¹⁹

⁶¹⁶ See Appendix 3 for a summary of recommendations from the *Report into Disclosure Regimes for Not-for-Profit Organisations*.

⁶¹⁷ Commonwealth, *Parliamentary Debates*, 18 June 2008, 2729 (Senator Lyn Allison).

⁶¹⁸ The Hon. Peter Costello MP, 'Government Response to Charities Definition Inquiry' (Media Release, No. 049, 29 August 2002) 1.

⁶¹⁹ Commonwealth, *Parliamentary Debates*, 18 June 2008, 2729 (Senator Lyn Allison). The Australian Consumers' Association (CHOICE is the association's public name) is a company limited by guarantee with no share capital. CHOICE diffuses information and advice to all consumers (and its members) about the standard, quality, properties and price of goods and services. Australian Consumers' Association, *Constitutional Objects* (May 2012) <<http://www.choice.com.au/about-us/governance.aspx>>.

Sometime in late 2007, CHOICE surveyed 240 of its subscribers, asking what they thought were important in a charity.⁶²⁰ CHOICE found that:

- 81 per cent did not know what proportion of their donation reached their favourite charity's beneficiaries (after fundraising costs and overheads were deducted);
- 94 per cent of the survey's respondents thought it was important to have information about a charity's administration and fundraising costs;
- 97 per cent surveyed thought it was important to have information about the effectiveness of a charity's work; and
- 90 per cent surveyed found it almost impossible to compare charities and, also, to know whether their donation was being used to its best effect.⁶²¹

CHOICE approached eleven unnamed large domestic and overseas charities to participate in this survey but only nine charities responded. The participating charitable organisations in CHOICE's survey were confined only to the charities' financial information. The method or framework that CHOICE used to compare the financial information of these participating charities was not disclosed. CHOICE reported that it was an impossible task to adequately compare the financial information of these participating charities due to each charity's financial information being structured in different ways.⁶²²

Responding to CHOICE's findings, the senators moved that an inquiry be referred to the Senate's Economics Committee to report on how to best improve governance and management of *all* not-for-profit organisations.⁶²³ The grounds outlined by the senators in their motion was to satisfy the wants of the donors' access to financial information rather than acknowledging the core issue, which is the declining public confidence and trust in the sector and organisations.

⁶²⁰ CHOICE's survey does not disclose how many CHOICE subscribers were asked to participate in this survey, nor does CHOICE disclose the make-up of the respondents such as, the number of women respondent, age-groups of respondents, etc.

⁶²¹ Alan Dooley, 'Guide to Donating to Charities – How Much of Your Donation is Gobbled up by Fundraising Fees and Expenses? 01. The Act of Giving CHOICE Guide and Review to Donating to Charities' <<http://www.choice.com.au/reviews-and-tests/money/investing/advice/charities.aspx>>.

⁶²² Alan Dooley, 'Guide to Donating to Charities – How Much of Your Donation is Gobbled up by Fundraising Fees and Expenses? 03. Survey of Charities CHOICE Guide and Review to Donating to Charities' <<http://www.choice.com.au/reviews-and-tests/money/investing/advice/charities/pages/survey%20of%charities.aspx>>.

⁶²³ Commonwealth, *Parliamentary Debates*, 18 June 2008, 2729 (Senator Lyn Allison).

6.2.2 *Terms of Reference*

The terms of reference for the Senate's Economic Committee ('the Committee') were framed to directly address the donors' want for information transparency. The Committee was tasked to explore models of regulation that would improve governance and management, and to examine other measures that would improve governance standards, accountability and transparency within not-for-profit organisations.⁶²⁴ The fiscal issues surrounding these organisations are significant; however, the scope of this inquiry should have been widened to search for reasons why public confidence and trust in the sector was declining, and find ways to re-build trust in the sector.

6.2.3 *Report's Findings*

The specific terms of reference resolved the Committee to having a limited scope to explore other issues that impact on the non-for-profit sector's effectiveness, and the Committee acknowledged this.⁶²⁵ It examined and provided recommendations on matters of fundraising, tax concessions and legal structures. The Committee did not considered legal duties or obligations as part of a governance framework for not-for-profit organisations, but it focused on financial reporting and models of regulation as the means to achieve transparency and accountability within the sector.

6.2.4 *Regulation*

The Committee acknowledged the overwhelming support from the sector to have better regulation.⁶²⁶ The issue for the Committee was to determine whether or not the not-for-profit sector should remain self-regulated, which, within the sector, has traditionally been the preferred model of regulation, due largely to the element of trustworthiness.⁶²⁷ The advantage of self-regulation is that it permits not-for-profits the freedom to decide for themselves how to effectively manage their organisations in a democratic way.⁶²⁸ The main feature of self-regulation

⁶²⁴ Standing Committee on Economics Report, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 5.

⁶²⁵ Standing Committee on Economics Report, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 8.

⁶²⁶ Standing Committee on Economics Report, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 37.

⁶²⁷ Jenny Harrow, 'Chasing Shadows? Perspectives on Self-Regulation in UK Charity Fundraising' (2006) 21 *Public Policy and Administration* 86, 88.

⁶²⁸ Fundraising Institute, Submission No. 107 to Standing Committee on Economics, *Inquiry into the Disclosure Regimes for Charities and Not-for-Profit Organisations*, 6 December 2008.

is a voluntary *Code of Conduct* that permits an organisation to define their own standards systems of governance and financial control, and establish ethics and principles for their members to follow.⁶²⁹ The Committee expressed their preference for a *Code of Conduct* by noting it could have a place in ‘a new system of regulation’.⁶³⁰ However, the Committee favoured a move away from self-regulation and strongly recommended the establishment of a national independent regulator for all forms of not-for-profit organisations.⁶³¹

The Committee showed that it had grasped the importance of needing a single national regulator.⁶³² The want for a national regulator derives from the Committee finding that the states-based system of regulation was complicated, making it difficult for not-for-profit organisations to function efficiently – particularly for those operating in more than one jurisdiction.⁶³³ The complicated state-based regulation of not-for-profit organisations emanates from the tensions between the legislative powers vested in the states and those vested in the Commonwealth.⁶³⁴ The Committee found that it would be prudent to create a new specialist federal legal structure through the referral of state and territory powers.⁶³⁵ The Committee believed that the creation of a new legal structure would simplify and provide ‘solid regulation’.⁶³⁶

⁶²⁹ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 37–38.

⁶³⁰ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 40.

⁶³¹ See Recommendation 3. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 45.

⁶³² The Commission accepted the advice of Professor Mark Lyons who insightfully stated that, without a regulator: governments will have a lack of knowledge about the sector; personal enrichment is more likely; not-for-profit organisations could be used to hide criminal activity; and the public would be less likely to inform authorities of charity abuse. Professor Mark Lyons, Submission No 112 to Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations*, 6 December 2008; Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 42.

⁶³³ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 40.

⁶³⁴ Within the not-for-profit context, the states and territories have the legislative power over incorporated associations, and a state’s Attorney General has control over charities. Whereas, the Commonwealth has legislative power over companies limited by guarantee. Not-for-profit organisations that operate across jurisdictions complained to the committee that not only is there poor regulation, but it is also difficult knowing and satisfying each jurisdiction’s requirements. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 68–70.

⁶³⁵ See Regulation 7. Standing Committee on Economic, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 77.

⁶³⁶ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 77.

Having made the determination to create a single national regulator, the Committee turned its attention on the regulator's function. The Committee examined the regulatory models of New Zealand and the United Kingdom, and clearly stated that those international models should not be copied.⁶³⁷ This resistance by the Committee derives from its own vision of how an Australian regulator of not-for-profit organisations should be. The Committee recommended that the new regulator be:⁶³⁸

- *A register* – All not-for-profit organisations would be required to be registered with the regulator. The regulator will issue the organisation with a unique identifying number, or allow the organisation to use its Australian Business Number ('ABN').⁶³⁹
- *A public interface* – The regulator would develop and maintain specific information about a not-for-profit organisation, which the public would have access to.
- *A data collector* – To collect and analyse annual data provided by not-for-profit organisations, which can be transferred to the ABS.
- *An educator* – To educate the public about the role of not-for-profit organisations.
- *An investigator* – To handle complaints relating to the operation of not-for-profit organisations.
- *A leader* – To develop best-practice standards for the operation of not-for-profit organisations.

Despite the Committee's desire for a regulatory model to be different from the one in the United Kingdom, these six functions can be found in the United Kingdom's Charity Commission. Chapter Seven of this thesis examines the United Kingdom's model of regulation. However, a point of difference between the two models is that the Committee's model would aim to serve the public's needs over the sector's needs. The United Kingdom's model of regulation not only protects the public's interest, but also serves to protect the integrity of individual not-for-profit

⁶³⁷ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 51–55.

⁶³⁸ See Recommendations 4, 5 and 6. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 59–60

⁶³⁹ The Committee held the view that this particular function would be unique to an Australian model of regulation, but this is not so. The United Kingdom's Charity Commission performs this particular function. Chapter Seven discusses the functions of the United Kingdom's Charity Commission. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 58.

organisations and, moreover, the sector.⁶⁴⁰ In fairness to the Committee, the United Kingdom has had substantial time to develop and refine their model, and Australia is playing catch-up to make the sector relevant in contemporary society.⁶⁴¹

6.2.5 Financial Reporting

Considering the issue of transparency, the Committee examined the current financial reporting requirements of not-for-profit organisations. It was dissatisfied with the significant reporting burden that not-for-profit organisations face, as well as the different requirements between jurisdictions.⁶⁴² Although the Committee was satisfied with the level of financial transparency relating to not-for-profits securing government grants,⁶⁴³ the reporting systems needed improvement. The Committee recommended a tiered reporting system based on an organisation's total annual revenue.⁶⁴⁴ This recommendation would see the implantation of a Standard Chart of Accounts developed by the Australian Centre for Philanthropy and Non-profit Studies, Queensland University of Technology.⁶⁴⁵

A Standard Chart of Accounts pertains to financial, numerical and narratives reporting which would better inform a donor about an organisation's financial activities, and also achieve transparency.⁶⁴⁶ Despite the Committee endorsing the use of the Standard Chart of Accounts, it did express reservations about its applicability to some forms of these organisations.⁶⁴⁷ The Committee believed that transparency could be achieved without standard accounts by requiring

⁶⁴⁰ Charity Commission, 'Strategic Plan 2012-2015, Vision, Mission and Values' 2-3 <http://www.charity-commission.gov.uk/Library/about_us/strategic_plan_2015.pdf>.

⁶⁴¹ Apart from England and Wales, regulatory frameworks for not-for-profit organisations can be found in Northern Ireland, Scotland and New Zealand. Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) pt IV.

⁶⁴² Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 103.

⁶⁴³ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 103.

⁶⁴⁴ See Recommendation 11. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 105.

⁶⁴⁵ See Recommendation 12. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 111-112.

⁶⁴⁶ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 111.

⁶⁴⁷ Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 111

organisations to disclose certain elements by narrative and numeric reporting.⁶⁴⁸ The Committee did not identify what these elements were, or the manner in which organisations of all forms and levels would disclose such information. Notwithstanding these concerns, the Committee suggested, as a matter of priority, that the federal government must further consult with the sector to implement a Standard Chart of Accounts.⁶⁴⁹ The federal government did not support all of the Committee's recommendations in its report;⁶⁵⁰ however, it did acknowledge the need for a single national regulator and a standard chart of accounts,⁶⁵¹ but held off making any further commitments to the Committee's report until the findings from the Productivity Commission and the Henry Tax Review were released.⁶⁵²

6.3 The Productivity Commission's Report

6.3.1 Background to the Productivity Commission's Report

It is commonly known that when the government of the day requests the Productivity Commission to furnish them with a report, the government is planning to take steps towards policy reform. In March 2009, the federal government requested the Productivity Commission to examine the contribution that the not-for-profit sector makes to Australian society.⁶⁵³ The commissioning of the report may also be seen more as action on their election commitment to have 'a strong and productive non-profit sector'.⁶⁵⁴

⁶⁴⁸ See recommendation 13. Standing Committee on Economics, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 112.

⁶⁴⁹ See recommendation 12. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008) 112.

⁶⁵⁰ The only recommendation, which the government agreed with, was to develop 'in principle' standard definitions and terminology for the sector. What the standard terms and definitions will be is dependent on the findings of the Productivity Commission and the Henry Review. Commonwealth Government, 'Commonwealth Government Response to the Standing Committee on Economics Senate Inquiry into Disclosure regimes for Charities and Not-for-Profit Organisations', 1
<http://www.aph.gov/senate/committee/economics_ctte/charities_08/gov_response.pdf>.

⁶⁵¹ See recommendations 3, 4, 5, 10, 11, 12, 13. Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008)

⁶⁵² Commonwealth Government, 'Commonwealth Government Response to the Standing Committee on Economics Senate Inquiry into Disclosure regimes for Charities and Not-for-Profit Organisations', 1–4
<http://www.aph.gov/senate/committee/economics_ctte/charities_08/gov_response.pdf>.

⁶⁵³ The Hon. Julia Gillard MP, The Hon. Chris Bowen MP and Senator Ursula Stephens MP, 'Productivity Commission to Review the Contribution of the Not-for-Profit Sector' (Joint Media Release, No. 17, 17 March 2009) 1.

⁶⁵⁴ The Hon. Julia Gillard MP, 'Strengthening the Non-Profit – Julia Gillard and Labor – Let's Move Australia Forward' (Media Release, No. unknown, undated) <<http://www.alp.org.au/getattachment/88a7eb81-8b47-4315-ad6e-c1c13c1963656/historic-reforms-to-australia-s-not-for-profits-wsec/>>.

6.3.2 *Terms of Reference*

Specifically, the Commission was tasked to, *inter se*:

1. improve on how to measure and consider measuring alternatives that will capture the not-for-profit sector's contribution to Australian society;
2. improve the use of measurements to shape government policy and programs;
3. identify unnecessary burdens or impediments on community organisations, including unnecessary or ineffective regulatory requirements and governance arrangements, while having regard to the need to maintain transparency and accountability;
4. consider options for improving the delivery of government-funded services by community organisations, including funding, contractual and reporting arrangements with government;
5. examine the changing relationships between government, business and community organisations; and
6. consider a broad definition of the not-for-profit sector to encompass most categories of not-for-profit organisations, including Australian-based international aid and development agencies.⁶⁵⁵

The main aim of the Productivity Commission's Report was to clearly exceed what other parliamentary inquiries tried to achieve. Where the previous parliamentary inquiries offered solutions confined to a selective type of problem, the Productivity Commission promised to be more encompassing by examining the many not-for-profit forms and the wide variety of activities that not-for-profit organisations undertake and, furthermore, provide action to remove obstacles to improve the sector's efficiency.⁶⁵⁶ Importantly, the Productivity Commission's Report was to provide the federal government with the necessary evidence-base to justify their reform policy. The reform recommended by the Productivity Commission was targeted at the whole not-for-profit sector, but specifically in the following areas:

- smarter regulation;
- improving accountability and governance;

⁶⁵⁵ The Hon. Julia Gillard MP, The Hon. Chris Bowen MP, and Senator The Hon. Ursula Stephens, MP 'Productivity Commission to Review the Contribution of the Not-for-Profit Sector' (Joint Media Release, No. 017, 17 March 2009) 2-3.

⁶⁵⁶ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) Terms of Reference IV-XXVI.

- improving data capture through advancing the current measuring frameworks; and
- facilitating development, innovation and relationship building.⁶⁵⁷

See Appendix 4 for a comprehensive summary of the Productivity Commission's Report's recommendations.

6.3.3 *The Productivity Commission's Findings*

To avoid repetition, the targeted areas of regulation, accountability and governance in the Productivity Commission's report do not greatly advance those solutions offered by the Disclosure Inquiry. However, the Commission's recommendations did not necessarily reflect those of the Inquiry – particularly in the areas of financial reporting and regulation.

6.3.4 *Regulation*

The need for sound regulation was a key area of reform marked 'urgent'.⁶⁵⁸ The Productivity Commission generally echoed the submissions and findings from the previous inquiries: that the current regulatory environment is unacceptable and complex.⁶⁵⁹ Adding their voice to this issue, the Productivity Commission criticised the state and territory governments for failing to improve the quality of regulation.⁶⁶⁰ The Commission considers the area of regulation to be made up of the following sub-matters: i) reporting requirements; ii) a regulator; iii) fundraising; iv) a new legal form; v) harmonisation of laws; and vi) tax status.⁶⁶¹ Similar to other inquiries, the Commission failed to consider legal duties as part of the governance framework.

⁶⁵⁷ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) LV.

⁶⁵⁸ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) xxxvi.

⁶⁵⁹ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 116.

⁶⁶⁰ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 115.

⁶⁶¹ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 113-114.

6.3.5 *A National Regulator*

Recommendations from previous inquiries supported the notion of a single national regulator for the not-for-profit sector, and the Productivity Committee agreed.⁶⁶² However, agreement on the shape and function of a national regulator is a point of debate. There was overwhelming support by the sector's stakeholders that a national regulator should reflect the form and function of the Charity Commission in the United Kingdom.⁶⁶³ However, the Productivity Commission's notion of a national registry did not necessarily reflect the desire of the sector's stakeholders. The Commission prefers a national registry to a national regulator.⁶⁶⁴

The Productivity Commission proposed that this statutory body be called the Registrar for Community and Charitable Purpose Organisation and would be established within the Australian Securities Investments Commission (ASIC).⁶⁶⁵ This new statutory body would be responsible for regulating companies limited by guarantee and indigenous corporations only.⁶⁶⁶ The function of the Registrar for Community and Charitable Purpose Organisations would be limited to registration, financial reporting, endorsing tax concessions and fundraising compliance.⁶⁶⁷ The Productivity Commission in justifying the creation of this statutory body thought that it would underpin public trust and increase public confidence in the entire not-for-profit sector.⁶⁶⁸

Increasing public confidence in the sector should be a priority for our policy makers, and a national registry is viewed as a step towards restoring public confidence by confirming an organisation's status to be a not-for-profit. However, this proposed framework is too narrow and thin on two grounds. First, the registrar will be a public record for only two forms of not-for-

⁶⁶² Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 117.

⁶⁶³ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 116.

⁶⁶⁴ The Productivity Committee is of the view that a regulator will not assist in the development of the not-for-profit sector. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 117.

⁶⁶⁵ See Recommendation 6.5. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 149.

⁶⁶⁶ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 111, 379.

⁶⁶⁷ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 111.

⁶⁶⁸ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 111.

profit organisations and ignores other forms.⁶⁶⁹ Secondly, the proposed model has not been constructed to facilitate transparency or to monitor the effectiveness of the not-for-profit sector and its organisations. Should the Registrar for Community and Charitable Purpose Organisations be given supervisory and regulatory powers, it would advance the public's confidence in the sector and achieve transparency.

6.3.6 Corporate and Financial Reporting Requirements

Along with the previous parliamentary inquiries, the Productivity Commission acknowledges financial reporting requirements across the different not-for-profit forms and jurisdictions are inconsistent.⁶⁷⁰ The Commission rightly called for the adoption of a national Standard Chart of Accounts to address this issue.⁶⁷¹ Further, the creation of a national Standard Chart of Accounts would encourage proportionate financial reporting regulation for all the legal forms of not-for-profits.⁶⁷²

Standardising the reporting system will provide the foundation for a single national portal.⁶⁷³ This portal will allow lodgement and access to corporate and financial information about companies limited by guarantee only. Access to this database will be for conducting a financial and corporate health checks for government contracting, and for the general public to be provided with valuable and meaningful information about the sector and organisations.⁶⁷⁴ State and territories would be called upon to harmonise their associations incorporated legislation to allow

⁶⁶⁹ State and territory governments have registries for incorporated associations; however, the other forms of not-for-profit organisations, such as unincorporated associations, foundations and cooperatives; have been ignored by the Productivity Commission and its recommendation for a national registry.

⁶⁷⁰ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 129.

⁶⁷¹ Standard Chart of Accounts is a standard of business reporting that aims to remove unnecessary and duplicated information from government forms by creating a common reporting language that is based on international standards and best practice. The approach taken by the Standard Chart of Accounts is to provide a common approach to capture accounting information for use of not-for-profit organisations and government agencies. The Standard of Accounts has been designed specifically for small to medium sized not-for-profit organisations that do not have an accounting department or a sophisticated accounting system. See Recommendation 6.5. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 134.

⁶⁷² Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 133.

⁶⁷³ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 135.

⁶⁷⁴ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 135.

the portal to link into the state's information systems.⁶⁷⁵ Establishing a national portal would seek to achieve the 'report once, use often' principle.⁶⁷⁶

Complementary to the introduction of a Standard Chart of Accounts, the Productivity Commission recommends the *Corporations Act 2001* (Cth) to be amended.⁶⁷⁷ Behind this recommendation is the Commission's finding that the rigours of the *Corporations Act 2001* (Cth) and the Australian Accounting Standards are burdensome for small organisations with limited resources.⁶⁷⁸ The Productivity Commission suggested that the government create a separate chapter in the *Corporations Act 2001* (Cth) for not-for-profit companies limited by guarantee.⁶⁷⁹ This separate chapter will outline the principles of proportionality in relation to reporting, fees and charges, and provide clearer rules on how to dispose of assets in the event of dissolution and prohibit payment of dividends to members of a company limited by guarantee.⁶⁸⁰

6.4 Conclusion

Australia's federal parliament had shown little interest in understanding the needs of the not-for-profit sector. However, in more recent times, it has commissioned numerous reports and inquiries to understand and reform the not-for-profit sector. From each inquiry a diverse range of issues affecting the not-for-profit sector and organisations has emerged, such as taxation, fundraising, measuring frameworks, government contracts and relations. At the core of these inquiries and reports is the lack of public confidence in the sector and the desire for not-for-profit organisations to be transparent in a manner akin to for-profit organisations. The Disclosure Inquiry and the Productivity Commission agreed that immediate action is needed to improve regulation by streamlining financial reporting obligations and introducing a statutory regulator – however, the Committee ignored the role that legal duties and obligations play in a governance framework.

⁶⁷⁵ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 135.

⁶⁷⁶ See Recommendation 6.6. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 135.

⁶⁷⁷ See Recommendation 6.1. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 128.

⁶⁷⁸ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 118, 120.

⁶⁷⁹ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 113.

⁶⁸⁰ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 134–135.

How the sector is to be regulated by a statutory federal agency, and how to implement financial reporting obligations for not-for-profit organisations have shown to be points of debate.

The Productivity Committee recommends that a national statutory body called the Registrar for Community and Charitable Purpose Organisations be established within the Australian Securities Investments Commission. The Registrar would be responsible only for companies limited by guarantee and indigenous corporations. On the other hand, the Committee of the Disclosure Inquiry recommended a national regulator be an independent statutory authority, which would be responsible for all forms of not-for-profit organisations and, furthermore, have investigative and regulative powers over the sector. The suggested model, called the Registrar for Community and Charitable Purpose Organisations, is devoid of these powers and serves the function of a registry for only two forms of not-for-profit organisations. Regardless of the shape that the national statutory body, there is an aim to improve governance of the sector through financial reporting obligations for not-for-profit sector.

The Productivity Commission and the Committee found inconsistencies across jurisdictions in the area of financial reporting. These inconsistencies were found to be caused by the tensions in the legislative powers vested in the states and the Commonwealth. The Committee recommended the formation of a new legal structure that would overcome these tensions. However, the Productivity Commission rejected the idea of a new legal structure and recommended that state incorporated association legislation relating to financial reporting be harmonised, and to allow a not-for-profit organisation to migrate into another form within the federal jurisdiction with ease. The harmonisation of state laws would include the introduction of a national Standard of Accounts and a tiered reporting system. The standardisation of financial reporting system would lead to the creation of a national portal, which would allow members of the public and governments to conduct a ‘corporate health check’ on individual organisations. The Committee and the Productivity Commission, in making their recommendations, examined the regulatory arrangements in the United Kingdom. Notwithstanding the overwhelming support to implement a model similar to the United Kingdom’s Charity Commission, the Committee and the Productivity Commission rejected this suggestion.

The Productivity Commission and the Committee, in rejecting the United Kingdom’s model, are pursuing their own vision. However, the basic recommendations made by the Committee and

the Productivity Commission, in relation to regulation and financial reporting, can also be found in the United Kingdom's Charity Commission.

CHAPTER 7: The United Kingdom's Attempt to Develop World's Best Practice for Not-for-Profits

*All developed countries, and many developing ones too, recognise the value of charitable and not-for-profit activity and the need to regulate it.*⁶⁸¹

7.0 Introduction

In mid 2001, the Blair Government initiated a major review of the United Kingdom's not-for-profit sector. The Strategy Unit was given the mandate by the prime minister to review the entire not-for-profit sector and to propose legal reforms that would modernise the not-for-profit sector in England and Wales.⁶⁸² The Strategy Unit delivered its report in September 2002, and proposed wide-ranging reforms to improve and modernise the legal and regulatory frameworks of the not-for-profit sector. The Blair government adopted and implemented all of the Strategy Unit's recommendations and, as such, the British regulatory model for not-for-profits has earned the status and recognition as world's best practice.⁶⁸³ Chapter Seven provides a brief historical overview of charity legislation in the United Kingdom, highlighting the different, and modern, not-for-profit organisational forms; it also examines the make-up and the valuable role the Charity Commission (the Commission) plays in regulating the not-for-profit sector and its organisations.

7.1 A Brief History of the United Kingdom's Charity Legislation

The protection and enforcement of charitable trusts was once the responsibility of the Attorney General⁶⁸⁴ until King James, by decree, statutorily assigned the role to an administrative body.⁶⁸⁵

⁶⁸¹ David Locke, 'Is Australia ready to change the way we treat our Not-for-Profit Sector? A view from the UK' (Speech delivered at the unnamed forum, Melbourne and Brisbane, June 2010) 4 <http://www.charity-commission.gov.au/About_us/About_the_Commission/Speeches/david_speech_0610.aspx>.

⁶⁸² Prime Minister's Strategy Unit (UK), 'Prime Minister Announces Voluntary Sector Review' (Press Release, 3 July 2001) <<http://www.strategy.gov.uk/output/Page3887.asp>>.

⁶⁸³ The Senate Economics Legislation Committee, Parliament of Australia, Canberra, Tax Laws Amendment (Public Benefit Test) Bill 2010, (September 2010) 4.34, 39.

⁶⁸⁴ The *parens patriae* jurisdiction of the Crown with respect to charities was devolved from the Lord Chancellor and vested in the Attorney General. *Ludlow Corp. v Greenhoe* (1827) 1 Bli. NS 17. Charitable trusts in Australia remain under the supervision of the states' Attorneys General, except in the Northern Territory. See *Attorney-*

This administrative body ended in 1803, and the government was, subsequently, given the responsibility to regulate and solve the problems of the day, which were: delay by charities lodging returns (sworn on oath to Parliament); abuse of charitable trusts; to reduce the expense of judicial action to remedy these troubles.⁶⁸⁶ The findings from the Brougham Inquiry of 1819–37 showed that the courts and the role of the Attorney General were inefficient in detecting the misuse of charitable funds, and this inquiry held that a better approach would be to establish a permanent Commission to supervise charities.⁶⁸⁷

The suggestion of a Commission was endorsed by parliament in the *Charitable Trusts Act 1858*.⁶⁸⁸ Over time, the Commission was provided with wide statutory power to supervise and support charities,⁶⁸⁹ and to be the official custodian.⁶⁹⁰ The modernisation of the not-for-profit sector in the United Kingdom and the Commission can be found in the *Charities Act 1993* (UK) and the *Charities Act 2006* (UK), which will be discussed further in this chapter.

As already mentioned, Prime Minister Blair commissioned a review of charity law and regulation in 2001.⁶⁹¹ All the recommendations from this review were accepted by the government and implemented through legislation or administrative action.⁶⁹² The *Charities Act 2006* (UK) was created to:

- modernise and restate charitable purposes;
- impose an express obligation on charities and trustees to ensure that they provided a public benefit;

General Act 2009 (Qld) s 7(e); *Charitable Trusts Act 1993* (NSW) pt 4; *Charitable Trusts Act 1993* (ACT) pt 2; *Charities Act 1978* (Vic) pt 2; *Trustee Act 1936* (SA) s 84E; *Variation of Trusts Act 1994* (Tas) s 7; *Charitable Trusts Act 1962* (WA) s 20.

⁶⁸⁵ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 69.

⁶⁸⁶ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 69.

⁶⁸⁷ Over four hundred charities were prosecuted, thereby prompting the need for an inquiry. Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 70.

⁶⁸⁸ The *Charitable Trust Act 1853* was amended in 1855 and 1860 and then consolidated in 1858. Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 70.

⁶⁸⁹ Strengthening the Commission's role and authority, the legislation followed the recommendation of the Woodfield Report. Secretary of State for the Home Department, *Charities: A Framework for the Future*, Whitepaper, Cmd 694 (May 1989); Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 197.

⁶⁹⁰ *Charities Act 1993* (UK) c 10, s 2.

⁶⁹¹ The Strategy Unit published the report entitled 'Private Action, Public Benefit – A View of Charities and the Wider Not-for-Profit Sector', which was open to public consultation from September 2002 to January 2003. Explanatory Notes to the *Charities Act 2006*, para 8; Cabinet Office, 'Private Action, Public Benefit – A View of Charities and the Wider Not-for-Profit Sector' (September 2002).

⁶⁹² Explanatory Notes to the *Charities Act 2006* (UK), para 10.

- amend the composition and function of the Commission;
- establish the Charity Tribunal; and
- improve the range of legal forms available to charities and social enterprise.⁶⁹³

Section 73 of the *Charities Act 2006* (UK) requires the Minister for the Cabinet Office to institute a review of this Act within five years after Royal Assent – this gives the impression that this area of law is forever changing. Recently, Lord Hodgson was appointed by the Cabinet Office to review the *Charities Act 2006* (UK).⁶⁹⁴ Lord Hodgson’s review will assess whether or not changes are needed to improve the legal and regulatory framework for charities and to determine the effectiveness of the 2006 Act.⁶⁹⁵ Lord Hodgson is not expected to submit his full report to Parliament until summer 2012,⁶⁹⁶ but this review has already seen changes to the *Charities Acts*.⁶⁹⁷

The *Charities Act 2011* (UK) repeals the *Recreational Charities Act 1958* (UK) and consolidates the *Charities Act 1993* (UK) and some provisions of the *Charities Act 2006* (UK).⁶⁹⁸ The 2011 Act has not made substantive changes to the law, nor does it introduces new policy.⁶⁹⁹ Although the *Charities Act 2011* (UK) received Royal Assent on 14 December 2011, the Act did not come into force until March 2012. This thesis will provide statutory provisions from the preceding charities’ legislation as well as the 2011 Act.

7.2 Overview of Legal Entities in England and Wales

To appreciate the extent of reforms undertaken within the United Kingdom’s not-for-profit sector, it is necessary to examine the legal entities individually.

⁶⁹³ Alison MacLennan, *Blackstone’s Guide to The Charities Act 2006* (Oxford University Press, 2007) Introduction, xvii.

⁶⁹⁴ HL Deb 23 November 2011, vol 23, col 1110.

⁶⁹⁵ Cabinet Office, ‘Review of the Charities Act 2006 – Terms of Reference’ <<http://www.cabinetoffice.gov.uk/resource-library/review-charities-act-2006-%E2%80%93-terms-reference.pdf>> 1.

⁶⁹⁶ The Hon Nick Hurd, Minister for Civil Society, ‘Review of Charity Law’ (Media Release, CAB 224-11, 8 November 2011) <<http://cabinetoffice.gov.uk/news/review-charitylaw>> 1.

⁶⁹⁷ *Charities Act 1992* (UK) c 10; *Charities Act 2006* (UK) c 50.

⁶⁹⁸ Charity Commission, ‘Charities Act 2011 – New Legislation receives Royal Assent’ <http://www.charity-commission.gov.uk/rss/updates/charities_act_2011.aspx>.

⁶⁹⁹ *Charities (Pre-consolidation Bill Amendments Order) 2011* (UK) SI 2011/1396 para 7.4

7.2.1 Charity

A charity within the English system is an institution (in the form of a trust) that has been established for a charitable purpose only.⁷⁰⁰ However this has now been given a broad ambit. A trust's charitable purpose must fall within any of the following descriptions:

- a) the prevention of relief of poverty;
- b) the advancement of education;
- c) the advancement of religion;⁷⁰¹
- d) the advancement of health, or the saving of the lives;⁷⁰²
- e) the advancement of citizenship or community development;⁷⁰³
- f) the advancement of the arts, culture, heritage or science;
- g) the advancement of amateur sport;⁷⁰⁴
- h) the advancement of human rights, conflict resolution or reconciliation, or the promotion of religious or racial harmony, or equality and diversity;
- i) the advancement of environmental protection or improvement;
- j) the relief of those in need by reason of youth, age, ill-health, disability, financial hardship or other disadvantage;⁷⁰⁵
- k) the advancement of animal welfare;
- l) the promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services, or ambulance services; or⁷⁰⁶
- m) any other purpose that is recognised as charitable purpose under existing charity law,⁷⁰⁷ or by virtue of section 1 of the *Recreational Charities Act*.⁷⁰⁸

⁷⁰⁰ *Charities Act 2006* (UK) c 50, s 1(1); *Charities Act 2011* (UK) c 25, s 1(1).

⁷⁰¹ Religion includes: (i) a belief in more than one God; and (ii) a religion that does not involve belief in a God. *Charities Act 2006* (UK) c 50, s 2 (3)(a); *Charities Act 2011* (UK) c 25, s 3(2)(a).

⁷⁰² The 'advancement of health' includes the prevention or relief of sickness, disease or human suffering. *Charities Act 2006* (UK) c 50, s 2(3)(b); *Charities Act 2011* (UK) c 25, s 3(2)(b).

⁷⁰³ 'Citizenship' or 'community development' includes: (i) rural or urban regeneration; and (ii) the promotion of civic responsibility, volunteering, the voluntary sector or the effectiveness or efficiency of charities. *Charities Act 2006* (UK) c 50, s 3(3)(c); *Charities Act 2011* (UK) c 25, s 3(2)(c).

⁷⁰⁴ 'Sport' means sports or games that promote health by involving physical or mental skill or exertion. *Charities Act 2006* (UK) c 50, s 2(3)(d); *Charities Act 2011* (UK) c 25, s 3(2)(d). However, a registered sporting club under schedule 18 of the *Finance Act 2002* (UK) c 23 and established for a charitable purpose cannot be a charity. *Charities Act 2006* (UK) c 50, s 5(3)-(4); *Charities Act 2011* (UK) c 25, s 3(2)(d).

⁷⁰⁵ This purpose includes relief given by the provision of accommodation or care to persons mentioned in this paragraph. *Charities Act 2006* (UK) c 50, s 2(3)(e); *Charities Act 2011* c 25, s 3(2)(e).

⁷⁰⁶ 'Fire and rescue services' means services provided by fire and rescue authorities under Part 2 of the *Fire and Rescue Services Act 2004* (UK). *Charities Act 2006* (UK) c 50, s 2(3)(f); *Charities Act 2011* (UK) c 25, s 3(2)(f).

The phrase ‘any other purpose’ in sub-paragraph (m) is to mean that an organisation will be a charitable if it can show that its purpose are analogous to, or within the spirit of, any purpose outlined in sub-paragraphs (a) to (l).⁷⁰⁹

This list expands the traditional four heads of charitable purpose taken from the 1601 *Statute of Elizabeth* and long-standing case law.⁷¹⁰ The expansion of charitable purposes also provides clarity to borderline cases.⁷¹¹ On a policy level, the new descriptions modernise charities to be more relevant to the needs of the twenty-first century, such as environmental protection and issues of human rights.⁷¹² However, despite expanding the parameters of charitable purposes, charities are still required to demonstrate a public benefit.⁷¹³

The public benefit test under section 3 requires a charity to demonstrate its aims are for the public benefit.⁷¹⁴ Underpinning the public benefit test are two key principles of: (i) there being and identifiable benefit; and (ii) the benefit must be to the public, or a sector of the public, which an organisation must also satisfy to achieve charitable status. Table 8 outlines the principles and the sub-principles of the public benefit test.

Determining charitable status for organisations is a decision made by the Commission.⁷¹⁵ The Commission in making their assessment of the ‘two-stage test’ (the purpose test and the public benefit test)⁷¹⁶ has indicated that it will not deviate from the long-standing charity law.⁷¹⁷ The

⁷⁰⁷ *Charities Act 2006* (UK) c 50, s 2(2); *Charities Act 2011* (UK) c 25, s 3(3). The ‘old law’ means the law relating to charity in England and Wales, which was in force before 1 April 2008. *Charities Act 2011* (UK) c 25, s 3(3)(4).

⁷⁰⁸ Section 1 provides that a trust will be charitable if it provides, or assist in the provision of, facilities for recreation or other leisure-time occupation, and if the facilities are provided in the interests of social welfare. *Recreational Charities Act 1958*, 6 & 7 Eliz 2; *Charities Act 2011* (UK) c 25, s 5. A ‘registered sporting club’ established for charitable purposes is treated as not being a charity. *Charities Act 2011* (UK) c 25, s 6.

⁷⁰⁹ *Charities Act 2006* (UK) c 50, s 2(4)(b)-(c); *Charities Act 2011* (UK) c 25, s 3(m)(ii)-(iii).

⁷¹⁰ The traditional heads of charitable purposes are: 1) the relief of poverty; 2) the advancement of education; 3) the advancement of religion; and 4) other purposes beneficial to the community. *Charitable Uses Act 1601* 43 Eliz 1, c 4.

⁷¹¹ Strategy Report, Private Action, Public Benefit – A Review of Charities and the Wider Not-for Profit Sector, September 2002, 36 < <http://www.cabinetoffice.gov.uk/media/cabinetoffice/strategy/assets/strat%20data.pdf>>.

⁷¹² Prior to these reforms, it was inconceivable under the Statute of Elizabeth and for the courts to treat an organisation such as Greenpeace as a charity. The expansion of charitable purpose is significant because it has made charities more relevant to today and the future.

⁷¹³ *Charities Act 2006* (UK) c 50, s 2(1)(b); *Charities Act 2011* (UK) c 25, s 4(1).

⁷¹⁴ *Charities Act 2006* (UK) c 50, s 3(1)-(2); *Charities Act 2011* (UK) c 25, s 4.

⁷¹⁵ Refer to 7.3.4 of this thesis for a details about the Commission’s functions.

⁷¹⁶ The charitable purpose test and the public benefit test will be refereed to as the ‘two-stage test’.

⁷¹⁷ Charity Commission, ‘Analysis of the law underpinning Charities and Public Benefit’ (December 2008) < <http://www.charity-commission.gov.uk/Library/guidance/lawpb1208.pdf>> Preface; Alison MacLennan,

onus remains on individual organisations to demonstrate to the Commission how their organisation's activities satisfy the two-stage test. The Commission in making its determination will also consider other extrinsic factors, such as the modern social and economic conditions in which the organisation intends to operate.⁷¹⁸

7.2.2 *Composition of a Charity*

Membership

The make-up of a charity is simple. A charity may have or not have a membership base, and members can be classed as voting or non-voting members. Voting members of a charity may either be corporate or individual members. Corporate members may include companies, local authorities, or any other public body or corporation where a nominated representative holds a right to vote at the charity's annual general meeting. A voting member may be a representative of another not-for-profit organisation or unincorporated charity. Individuals acting in the capacity of a trustee, director, or any other role on the governing body of the charity, are not classified as members.⁷¹⁹

Trustees

Charity trustees are individuals who have the responsibility and the general control to manage and administer the organisation.⁷²⁰ Trustees can also be known as directors, board members, governors, committee members, and a connected person. Many trustees are volunteers, and it is not uncommon for professional trustees to be involved with charities.⁷²¹ Furthermore, there are also nominative and ex-officio trustees. A nominative trustee is appointed by another

Blackstone's Guide to The Charities Act 2006 (Oxford University Press, 2007) 13-14; Charity Commission, Decision of the Charity Commissioners For England and Wales Made on the 30 January 2003, Application for Registration of the Wolf Trust (Formerly Known as Wild Bite) para, 4.2-5.5, 2 <<http://www.charity-commission.gov.uk/Library/start/wolftrustdecision.pdf>>.

⁷¹⁸ Charity Commission, 'Analysis of the Law Underpinning Charities and Public Benefit' (December 2008) <http://www.charity-commission.gov.uk/Library/guidance/lawpb1208.pdf>; Charity Commission, Decision of the Charity Commissioners for England and Wales, Application for Registration of the Wolf Trust (Formerly known as Wild Bite), 30 January 2003, para 2, <<http://www.charity-commission.gov.uk/Library/start/wolftrustdecision.pdf>>; Charity Commission, Application for Registration of Good News for Israel Decision made on 5 February 2004, para 2.1, 1 <<http://www.charity-commission.gov.uk/Library/start/gnfydecision.pdf>>.

⁷¹⁹ Charity Commission, 'RS7 – Membership Charities' (March 2004) <<http://www.charity-commission.gov.uk/publications/rs7.aspx>>5-7.

⁷²⁰ *Charities Act 1993* (UK) c 50, s 97; *Charities Act 2011* (UK) c 25, s 177.

⁷²¹ Charity Commission, 'CC3 – The Essential Trustee: What you Need to Know' (February 2008) <<http://www.charitycommission.gov.uk/publications/cc3.aspx>> 4.

organisation, and an ex-officio trustee is one by virtue of their office – for example, a vicar of a parish.⁷²² Regardless of the individual's title or appointment, all trustees have the same responsibilities and duties.

7.2.3 *A Trustee's Duties and Responsibilities*

When individuals take on the role of a trustee they accept the responsibility of directing the charity's affairs that will deliver outcomes that benefits the public.⁷²³ To remain true to the charitable purpose, trustees must ensure that they and their charities comply with all United Kingdom's laws (specifically, charity law) and any other requirements of the Charity Commission.⁷²⁴ Additionally, a trustee is expected to meet a number of general and specific legal duties.

Generally, trustees have a duty of prudence and a duty of care. To satisfy the duty of prudence they must ensure their charity is and remains solvent, and to reasonably use charitable funds and assets only to further the charity's purpose and interests.⁷²⁵ Trustees must take special care when investing or borrowing funds for their charities.⁷²⁶ Furthermore, they must avoid undertaking activities that might place their charity's funds, property, assets or reputation at undue risk.⁷²⁷

With respect to duty of care, the trustees must use reasonable care and skill to ensure their charity is well run and efficient by employing their personal skills and experience.⁷²⁸ Where a material risk is present, trustees would breach their duty of care if they do not consider seeking

⁷²² Charity Commission, 'A Guide to Conflicts for Charity Trustees' (February 2011) <http://www.charitycommission.gov.uk/Charity_requirements_guidance/Charity_governance/conflicts.aspx> 9-10.

⁷²³ Charity Commission, 'CC3 – The Essential Trustee: What you Need to Know' (February 2008) <<http://www.charitycommission.gov.uk/publications/cc3.aspx>>, 7.

⁷²⁴ Counter-terrorism laws also have an impact on charities and trustees. Charity Commission, 'Charity Law Duties and Responsibilities, Compliance Toolkit: Protecting Charities from Harm, Chapter 1: Charities and Terrorism Module 8' <http://www.charity-commission.gov.uk/our_regulatory_activity/counter_terrorism_work/tkch1mod8.aspx> 1.

⁷²⁵ Charity Commission, 'CC3a – The Essential Trustee: An Introduction' (January 2007) <<http://www.charity-commission.gov.uk/Publications/cc3a.aspx>> 2.

⁷²⁶ Charity Commission, 'CC3a – The Essential Trustee: An Introduction' (January 2007) <<http://www.charity-commission.gov.uk/Publications/cc3a.aspx>> 2.

⁷²⁷ Charity Commission, 'CC3a – The Essential Trustee: An Introduction' (January 2007) <<http://www.charity-commission.gov.uk/Publications/cc3a.aspx>>, 2.

⁷²⁸ Charity Commission, 'CC3a – The Essential Trustee: An Introduction' (January 2007) <<http://www.charity-commission.gov.uk/Publications/cc3a.aspx>>, 2.

external professional advice regarding the specific risk.⁷²⁹ To further satisfy this duty, trustees must not engage in conduct that would amount to misconduct in the administration of their charities, and that would subsequently harm the public confidence in them. Additionally, trustees must fulfil specific duties that relate to the running of their charity.

To avoid improper behaviour, trustees have a duty to avoid conflicts of interest. No trustee should be in receipt of an unauthorised benefit and, therefore a trustee should not be in a position where his or her personal interests and the duty to the charity are in conflict.⁷³⁰ However, trustees may keep a potential benefit if the conflict is transparent. To uphold a trustee's duty of trust and loyalty, and to be seen as transparent, the conflict must be properly and openly managed. To manage a conflict of interest adequately, a trustee must declare his or her interest at the commencement of the Trustees' meeting, retreat from taking part in the discussion during the meeting, and outline the interest in the charity's register of interest.⁷³¹

Complying with the requirements of the Charity Commission is another specific duty of a trustee. The Commission requires a charity to be registered and to provide Annual Returns and Trustees' Annual Reports and Accounts to the Commission.⁷³² A trustee has a duty to ensure that the charity's accounting records are kept sufficiently, which shows and explains all the charity's transactions.⁷³³ Records of financial transactions undertaken by the charity provide the basis for a trustee's annual statement and report.⁷³⁴

Pursuant to the *Trustee Act*,⁷³⁵ a trustee has wide statutory powers to facilitate proper administration of trusts and to safeguards the interests of beneficiaries.⁷³⁶ For trustees to achieve

⁷²⁹ Charity Commission, 'CC3a – The Essential Trustee: An Introduction' (January 2007) < <http://www.charity-commission.gov.uk/Publications/cc3a.aspx> > 2-3.

⁷³⁰ Charity Commission, 'CC3a – The Essential Trustee: An Introduction' (January 2007) < <http://www.charity-commission.gov.uk/Publications/cc3a.aspx> > 2.

⁷³¹ Charity Commission, 'A Guide to Conflicts of Interest for Charity Trustees' (February 2011) < http://www.charitycommission.gov.uk/Charity_requirements_guidance/Charity_governance/Good_governance/conflicts.aspx > 2-9.

⁷³² *Charities Act 2006* (UK) c 50, s 3B(1); *Charities Act 2011* (UK) c 25, s 30(1).

⁷³³ *Charities Act 1993* (UK) c 10, s 41; *Charities Act 2011* (UK) c 25, s 130.

⁷³⁴ *Charities Act 1993* (UK) c 10, s 42; *The Charities (Accounts and Reports) Regulations 2008* (UK) SI 2009/1942 reg 8; *Charities Act 2011* (UK) c 25, s 131-132; Charity Commission, 'CC15b – Charity Reporting and Accounting: The Essentials' (April 2009) < <http://www.charity-commission.gov.uk/Publications/cc15b.aspx> > 5. A Trustees' Annual Report is only necessary if the registered charity has a gross income that exceeds £10,000.00. *Charities Act 1993* (UK) c 10, s 45.

⁷³⁵ *2000* (UK) c 29.

⁷³⁶ Explanatory Notes, *Trustee Act 2000* (UK) c 29, 4-5, 1.

this, section 1 defines a statutory duty of care for them.⁷³⁷ To comply with section 1, trustees must show their skill and care is reasonable in the circumstances, thus making allowances for a trustee's special knowledge, experience or professional status.⁷³⁸ This duty of care is applicable where trustees are exercising their investment power for the following activities:

- investing trust property;
- investing or reviewing investments;
- acquiring or managing land;
- appointing or reviewing the appointment of an agent, nominee or custodian;
- compounding liabilities;
- insuring trust property; and
- dealing with reversionary interests, valuations and audits.⁷³⁹

Where a trust instrument does not provide a trustee with the power to invest, a default power of investment is provided in section 3.⁷⁴⁰ The statutory power to invest a trust's assets is considered to be the same if an individual trustee owned the assets rather than holding them on trust.⁷⁴¹ Without diminishing the obligations of trustees, they are under an express duty to have regard to the best interests of the trust's beneficiaries.⁷⁴² Therefore, these duties and obligations require a trustee (or more so the individual) to dedicate enough of his or her time to meet their legal duties and responsibilities.

7.2.4 *Charitable Incorporated Organisations*

Another innovative reform under the *Charities Act 2006* (UK) was the creation of a new incorporated charitable form, the charitable incorporated organisation.⁷⁴³ The charitable incorporated organisation (CIO) provides the benefit of incorporation by creating a legal

⁷³⁷ *Trustee Act 2000* (UK) c 29.

⁷³⁸ *Trustee Act 2000* (UK) c 29, s 1(1)(a)–(b).

⁷³⁹ *Trustee Act 2000* (UK) c 29, s 2, sch 1. Dealing with reversionary interests, valuations and audits occur under section 22(1) or (3) *Trustee Act 1925* (UK).

⁷⁴⁰ *Trustee Act 2000* (UK) c 29.

⁷⁴¹ *Trustee Act 2000* (UK) c 29, s 3–7.

⁷⁴² *Trustee Act 2000* (UK) c 29, s 8; Explanatory Notes, *Trustee Act 2000* (UK), 6.2.

⁷⁴³ *Charities Act 2006* (UK) c 50, s 43; *Charities Act 2011* (UK) c 25, s 204.

personality for a charity, and provides trustees with limited liability⁷⁴⁴ – designed to avoid duplication of the registration process and reporting requirements for charitable companies.⁷⁴⁵ A CIO could easily be considered (*prime facie*) to be the same as an incorporated association, but such a simple thought can be misleading.

7.2.5 *Composition of a Charitable Incorporated Organisation*

The similarities between a CIO and an incorporated association are few. Both entities are bodies corporate that have limited liability and a constitution.⁷⁴⁶ The respective constitutions are similar in that the CIO document makes provisions for:

- a membership base;⁷⁴⁷
- eligibility criteria for membership;
- the appointment and eligibility (including conditions) of an appointment of a charity trustee; and
- directions about the application of property upon dissolution of the CIO.⁷⁴⁸

This last prescribed feature is not outlined in an incorporated association's constitution, and must resort to the relevant legislation for guidance on the issue.⁷⁴⁹

The Commission will decide whether a non-profit organisation is eligible to become a CIO, and the Commission registers a CIO as a charity.⁷⁵⁰ To be registered as a charity and to gain charitable status, the Commission must be satisfied that the CIO meets the two-stage test.⁷⁵¹

⁷⁴⁴ Charity Commission, 'Charities Act 2006 – What Trustees Need to Know' <http://www.charity-commission.gov.uk/Charity_requirements_guidance/ccpubs3.aspx> 15-16.

⁷⁴⁵ A charitable company (limited by guarantee) is required to be registered and meet reporting requirements under company law with Companies House. Hubert Picarda QC, 'Harmonising Nonprofit Law in the EU' in Klaus Hopt and Thomas Von Hippel (eds), *International Corporate Law and Financial Market Regulation – Comparative Corporate Governance of Non-Profit Organisations* (Cambridge University Press, 2010) 185. Further, a charitable company, a community interested company, and a registered society under the *Industrial and Provident Societies Act 1965* (UK) are encouraged to convert to the CIO structure. *Charities Act 2006* (UK) c 50, s 69G(1), 69J, sch 7; *Charities Act 2011* (UK) c 25, s 228.

⁷⁴⁶ *Charities Act 1993* (UK) c 10, s 69A; *Charities Act 2006* (UK) c 50, sch 7; *Charities Act 2011* (UK) c 25, s 205. Members of a CIO are not liable to contribute to assets of the CIO if it is wound up. *Charities Act 1993* (UK) c 10, s 69A(6)(a); *Charities Act 2011* (UK) c 25, s 205(3).

⁷⁴⁷ *Charities Act 1993* (UK) c 10, s 69A(5); *Charities Act 2011* (UK) c 25, s 206(2).

⁷⁴⁸ *Charities Act 1993* (UK) c 10, s 69B(2); *Charities Act 2011* (UK) c 25, s 206(2)(c).

⁷⁴⁹ See *Associations Incorporation Act 1981* (Qld) s 4(9); *Associations Incorporation Act 2009* (NSW) s 65; *Associations Incorporation Act (ACT) 1991* s 92; *Associations Incorporation Act 1964* (Tas) s 22; *Associations Incorporation Act 1985* (SA) s 46; *Associations Incorporation Act 1987* (WA) s 30; *Associations Incorporation (Amendment) Act 2000* (Vic) s 33A; *Associations Incorporation Amendment Act 2010* (Vic) s 23; *Associations Incorporation Reform Act 2012* (Vic) s 23.

Membership

Divergence between the two forms is seen when comparing the qualification to become incorporated and the membership requirements. An incorporated association requires a prescribed number of members to be eligible for incorporation, whereas a CIO needs only one member.⁷⁵²

Individuals on the executive or management committee of an incorporated association are required to be a member of the association, whereas a trustee of a CIO is not required to be a member of the CIO.⁷⁵³

7.2.6 CIO Trustees' Duties and Members' Duties

All trustees of a CIO performing their functions and exercising their powers must do so with care and skill that is reasonable in the circumstances.⁷⁵⁴ Where a trustee is exercising reasonable skill and care, regard will be given to the trustee's special knowledge or experience that the trustee purports to have.⁷⁵⁵

Furthermore, an individual in the position of a trustee must not benefit personally (either directly or indirectly) from any arrangement or transaction entered into by the CIO.⁷⁵⁶ A trustee is required to disclose any material interest before the CIO enters into the transaction, or arrangement.⁷⁵⁷ Regarding a member's duty, section 220 requires all members of a CIO to exercise their powers in good faith, where it is likely to further the purposes of the CIO.⁷⁵⁸

⁷⁵⁰ *Charities Act 2006* (UK) c 50, sch 7, s 69E(1); *Charities Act 2011* (UK) c 25, s 209(1).

⁷⁵¹ *Charities Act 2006* (UK) c 50, s 3; *Charities Act 2011* (UK) c 25, s 208; Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 54.

⁷⁵² *Charities Act 2006* (UK) c 50, sch 7, s 69A(5); *Charities Act 2011* (UK) c 25, s 205(2)(c). See 4.3.3 for an outline of the statutory requirements for membership to an incorporated association.

⁷⁵³ *Charities Act 1993* (UK) c 10, s 69B(6); *Charities Act 2011* (UK) c 25, s 206(6)(b). It is common in England for charities and CIOs to appoint professional trustees rather than rely on the membership base to appoint a trustee.

⁷⁵⁴ *Charities Act 2011* (UK) c 25, s 221(2).

⁷⁵⁵ *Charities Act 2011* (UK) c 25, s 221(2)(a).

⁷⁵⁶ *Charities Act 2011* (UK) c 25, s 222(1)-(2).

⁷⁵⁷ *Charities Act 2011* (UK) c 25, s 222(1).

⁷⁵⁸ *Charities Act 2011* (UK) c 25.

7.2.7 Charitable Unincorporated Associations/Charities

A charitable unincorporated association (CUA) is described as a group of people that co-operate and play out certain administrative roles to further their organisation.⁷⁵⁹ A CUA can either be a trust or association, but it cannot be a company with a legal personality.⁷⁶⁰ Similar to the other forms of not-for-profit organisations in the United Kingdom, a CUA must be registered with the Commission, which encourages organisations to consider the CUA structure.⁷⁶¹ The structure of a CUA is encouraged where an organisation:

- has a membership base;
- the membership base represents the views of local residents, local councils and other bodies that need to be represented through a membership base, or are users of facilities;
- the organisation's object is to be carried out wholly or partly by the members;
- trustees are elected by the members;
- elected trustees hold office for a fixed period of time (e.g. a year);
- is a local branch of a national charity; or
- is small in terms of assets (income less than £5,000).⁷⁶²

Despite the requirement for a CUA to be registered with the Commission, this does not suggest that a CUA becomes a body corporate upon registration.⁷⁶³ Through registration, a CUA falls under the Commission's supervision. The Commission plays an important role in facilitating the powers of a UCA's trustee. A trustee of a UCA has the power to conduct the following:⁷⁶⁴

⁷⁵⁹ Charity Commission, 'CC22 – Choosing and Preparing a Governing Document' <<http://www.charitycommission.gov.uk/publications/cc22.aspx#9>> 6.

⁷⁶⁰ An ACU cannot enter into contracts in their own names. Charity Commission, 'Glossary, Charities Act 2006 – What Trustees Need to Know' <http://www.charity-commission.gov.uk/Charity_requirements_guidance/ccpubs3.aspx> 46.

⁷⁶¹ Where a CUA is an exempted charity there is no requirement to be registered with the Commission. Charity Commission, 'CC22 – Choosing and Preparing a Governing Document' <<http://www.charitycommission.gov.uk/publications/cc22.aspx#9>>, 6.

⁷⁶² Charity Commission, 'CC22 – Choosing and Preparing a Governing Document' <<http://www.charitycommission.gov.uk/publications/cc22.aspx#9>> 7.

⁷⁶³ Pursuant to sections 50 and 52 of the *Charities Act 1993* (UK) trustees may apply to the Commission for a certificate of incorporation as a body corporate. Once the Commission grants the certificate, the charity becomes a body corporate. *Charities Act 1993* (UK) c 10, s 50(3)(a); *Charities Act 2011* (UK) c 25, s 251(1).

⁷⁶⁴ *Charities Act 2006* (UK) c 50, ch, 10; *Charities Act 2011* (UK) c 25, ch 13.

- transfer property and permanent endowment;⁷⁶⁵
- resolve and replace a UCA's purposes;⁷⁶⁶
- modify the administration procedures of a UCA;⁷⁶⁷ and
- spend available capital.⁷⁶⁸

Despite the Commission supervising UCAs, the known legal uncertainties and troubles with the unincorporated form still remain.

7.2.8 *Community Interest Companies*

The community interest company (CIC) was created in 2005 for organisations that did not want to be a charity, but wished to pursue altruistic activities. At the time of creation, the CIC structure was earmarked to be an effective legal form for social enterprises.⁷⁶⁹ Specifically, the design behind the CIC structure allows for people who would like to establish or conduct a business that trades with a social purpose, or for a community benefit. Common activities carried out by a CIC are community medical practices, environment projects, childcare, arts and education projects.⁷⁷⁰ Like any other not-for-profit organisation, a CIC cannot be formed or used for the personal gain of an individual or a group of people, such as investors – nor can they be formed to support political purposes.⁷⁷¹ However, if the organisation has a charitable status, it may apply to registered as a CIC subsidiary company with Companies House.⁷⁷²

⁷⁶⁵ *Charities Act 1993* (UK) c 10, s 74, 74B; *Charities Act 2006* (UK) c 50, s 40; *Charities Act 2011* (UK) c 25, s 268.

⁷⁶⁶ *Charities Act 1993* (UK) c 10, s 74C; *Charities Act 2006* (UK) c 50, s 40; *Charities Act 2011* (UK) c 25, s 275.

⁷⁶⁷ *Charities Act 1993* (UK) c 10, s 74D; *Charities Act 2006* (UK) c 50, s 40; *Charities Act 2011* (UK) c 25, s 280.

⁷⁶⁸ *Charities Act 1993* (UK) c 10, s 75, 75A–75B; *Charities Act 2006* (UK) c 50, s 40; *Charities Act 2011* (UK) c 25, s 281. Larger unincorporated charities (annual income of over £1,000, or market value of the permanent endowment over £10,000) must obtain the Commission's consent to spend the endowment.

⁷⁶⁹ Sara Burgess, *The Regulator of Community Interest Companies* <[http://www.cicregulator.gov.uk/guidance/Chapter%201%20-%20October%202009%20\(version%204%20final\).pdf](http://www.cicregulator.gov.uk/guidance/Chapter%201%20-%20October%202009%20(version%204%20final).pdf)> 2.

⁷⁷⁰ Community Interest Company Regulator, 'Chapter 4: Creating a CIC' (20 October 2009) <<http://www.cicregulator.gov.uk/guidance/CIC%20%20ch%204%20Oct%202009%20version%209%20final.pdf>>.

⁷⁷¹ Community Interest Company Regulator, 'Chapter 7: Community Interest Companies' <<http://www.companieshouse.gov.uk/about/gbhtml/gp1.shtml#ch7>>.

⁷⁷² Community Interest Company Regulator, 'About Us: Community Interest Companies (CICs)' <<http://www.cicregulator.gov.uk/aboutUs.shtml>>.

A CIC enjoys limited liability, and this structure can be incorporated as a new company, or an existing one that can be converted.⁷⁷³ The forms that a CIC may take are: a company limited by guarantee; a private company limited by shares; or a public company limited by shares.⁷⁷⁴ Before obtaining company status, the CIC regulator must be satisfied the company has satisfied the asset lock test and the community interest test.⁷⁷⁵

There is an inter-relationship between the asset lock test and the community interest test.⁷⁷⁶ For a company to satisfy the community interest test, ‘a reasonable person might consider its activities are being carried on for the benefit of the community.’⁷⁷⁷ The asset lock test ensures that the company’s assets generated from its activities (including any profits or surplus) are used for the benefit of the community. The company’s articles of association must state ‘the company shall not transfer any of its assets for full consideration (market value)’.⁷⁷⁸

A CIC is allowed to pay dividends to shareholders, but this depends on the company’s article, which the company adopts from *The Community Interest Company (Amendment) Regulations 2009* (UK). A CIC with share capital that adopts Schedule 2’s articles of association is allowed to pay dividends to an asset-locked body, and a dividend payment is only made with the consent of the Regulator.⁷⁷⁹ Alternatively, if a CIC with share capital has Schedule 3 as its articles of association, dividends maybe paid to shareholders who are not asset-locked bodies.⁷⁸⁰ A dividend

⁷⁷³ A limited company registered with the Registrar of Companies for England and Wales, Northern Ireland or Scotland.

⁷⁷⁴ *Companies Act 2006* (UK) c 46, ch 1, s 6; Company Interest Regulator, ‘Introduction – Community Interest Companies’ <[http://www.cicregulator.gov.uk/guidance/Chapter%201%20-%20October%202009%20\(version%204%20final\).pdf](http://www.cicregulator.gov.uk/guidance/Chapter%201%20-%20October%202009%20(version%204%20final).pdf)> 9.

⁷⁷⁵ Community Interest Regulator, ‘Chapter 6: The Asset Lock’ (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 3.

⁷⁷⁶ Community Interest Regulator, ‘Chapter 6: The Asset Lock’ (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 3.

⁷⁷⁷ *Companies (Audit and Investigations and Community Enterprise) Act 2004* (UK) c 17, s 35; Community Interest Regulator, ‘Chapter 6: The Asset Lock’ (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 3. ‘Community’ means either the community or population as a whole, or a definable sector or group of people in the United Kingdom or elsewhere. Any group of individuals constitutes a community if they share a common characteristic that a reasonable person could distinguish from other members of the community, or a section of the community. *Community Interest Company (Amendment) Regulations 2009* (UK) SI 2008/629, reg 5.

⁷⁷⁸ Community Interest Regulator, ‘Chapter 6: The Asset Lock’ (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 26.

⁷⁷⁹ *Community Interest Company (Amendment) Regulations 2009* (UK) SI 2008/629.

⁷⁸⁰ *Community Interest Company (Amendment) Regulations 2009* (UK) SI 2008/629.

payment to a private financial investor is subject to a dividend cap.⁷⁸¹ However, a dividend cap does not apply to those paid to certain asset-locked bodies.

A dividend cap is to achieve a balance that encourages people to invest, and to ensure assets and profits are used for the benefit of the community.⁷⁸² Further, the dividend cap ensures that a paid dividend is proportionate to the amount invested and the CIC's profits.⁷⁸³

Composition of CICs

Private CICs must have at least one director, but a CIC public company must have at least two.⁷⁸⁴

A CIC, like any other private company, has the option to appoint or not a company secretary, or have employees.⁷⁸⁵

Membership

Usually, members of a CIC are its shareholders, providing this is permissible under the CIC's articles of the association.⁷⁸⁶ A CIC that is limited by guarantee describes its members as subscribing guarantors. The membership base of a CIC has the control and the general responsibility for decision-making, such as appointing and dismissing directors.⁷⁸⁷

A Director's Duties

Directors of a CIC, like any other company director, are subject to common law, equitable and statutory duties. The scope and nature of a director's general duties fall under the *Companies Act*,⁷⁸⁸ which are based on certain common law rules and equitable principles.⁷⁸⁹ A director has a

⁷⁸¹ Community Interest Regulator, 'Chapter 6: The Asset Lock' (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 4.

⁷⁸² Community Interest Regulator, 'Chapter 6: The Asset Lock' (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 5-6. There are three elements to a dividend: (i) maximum share; (ii) aggregate; and (iii) a carried forward unused dividend. Community Interest Regulator, 'Chapter 6: The Asset Lock' (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 6-8.

⁷⁸³ Community Interest Regulator, 'Chapter 6: The Asset Lock' (October 2009) <<http://www.cicregulator.gov.uk/guidance/Chapter%206%20-%20Feb%202010.pdf>> 6.

⁷⁸⁴ *Companies Act 2006* (UK) c 46, s 154.

⁷⁸⁵ *Companies Act 2006* (UK) c 46, s 270; Community Interest Company Regulator, 'Chapter 9: Corporate Governance' (October 2009) <[http://www.cicregulator.gov.uk/guidance/Chapter%209%20-%20October%202009%20\(version%205%20Final\).pdf](http://www.cicregulator.gov.uk/guidance/Chapter%209%20-%20October%202009%20(version%205%20Final).pdf)> 9.1.

⁷⁸⁶ *Companies Act 2006* (UK) c 46, s 112.

⁷⁸⁷ Community Interest Company Regulator, 'Chapter 9: Corporate Governance' (October 2009) <[http://www.cicregulator.gov.uk/guidance/Chapter%209%20-%20October%202009%20\(version%205%20Final\).pdf](http://www.cicregulator.gov.uk/guidance/Chapter%209%20-%20October%202009%20(version%205%20Final).pdf)> 9.2.

⁷⁸⁸ *2006* (UK) c 46.

general duty to act in accordance with the company's constitution and to exercise powers for conferred purposes.⁷⁹⁰

Further, a company director has a duty to promote the success of the company, and do so by acting in good faith that benefits its members as a whole,⁷⁹¹ having regard to the following:

- a) the likely long-term consequences of any decision;
- b) the interests of the company's employees;
- c) the need to foster the company's business relationships with suppliers, customers and others;
- d) the impact of the company's operation on the community and the environment;
- e) the desirability of the company maintaining a reputation for high standards of business conduct; and
- f) the need to act fairly, as between members of the company.⁷⁹²

A director in certain circumstances has a duty to consider or act in the interests of the company's creditors.⁷⁹³ A director exercising independent judgment, must not infringe upon any agreement, or the company's constitution.⁷⁹⁴

Furthermore, a director has the duty to exercise reasonable care, skill and diligence.⁷⁹⁵ The meaning of exercising this specific duty is objective. Consideration is given to what a reasonable diligent person, with the general knowledge, skill and experience of the director, could be reasonably expected to do while carrying out the function of a director.⁷⁹⁶

Further, directors has a duty to avoid a situation where they have, or can have a direct or indirect interest, or possibly a conflict with the company's interests.⁷⁹⁷ The duty to avoid conflicts of interest refers to the exploitation of any property, information or opportunity. Whether a company could take advantage of the property, information or opportunity it is considered

⁷⁸⁹ *Companies Act 2006* (UK) c 46, s 170(3)–(5).

⁷⁹⁰ *Companies Act 2006* (UK) c 46, s 171.

⁷⁹¹ *Companies Act 2006* (UK) c 46, s 172(1).

⁷⁹² *Companies Act 2006* (UK) c 46, s 172(1)(a)–(f).

⁷⁹³ *Companies Act 2006* (UK) c 46, s 172(3).

⁷⁹⁴ *Companies Act 2006* (UK) c 46, s 173.

⁷⁹⁵ *Companies Act 2006* (UK) c 46, s 174.

⁷⁹⁶ *Companies Act 2006* (UK) c 46, s 174(2).

⁷⁹⁷ *Companies Act 2006* (UK) c 46, s 175(1).

immaterial.⁷⁹⁸ An exception to this duty relates to a transaction, or arrangement a director has with the company.⁷⁹⁹ A further exception to this duty is where there is a situation that cannot be reasonably regarded as giving rise to a conflict of interest, or if the matter is authorised by other directors.⁸⁰⁰ Authorisation given by the directors is only effective if the quorum requirements are satisfactorily met and the matter agreed without the director's vote.⁸⁰¹

The duty to avoid conflict of interests does not apply to a company that it is a charity. Where a conflict of interest arises in relation to a transaction or arrangement with the company, this duty does not apply to descriptions of transactions or arrangements specified in the company's articles.⁸⁰² The authorisation given by the directors of a charity enables them to authorise such matters in accordance with the constitution.⁸⁰³

A company director has a duty not to accept a benefit from a third party;⁸⁰⁴ that is, a person, or a person acting behalf of another that is other than the company or an associated body corporate.⁸⁰⁵

7.2.9 Regulator for CICs

The office known as the Regulator of Community Interest Companies is established under the *Companies (Audit, Investigations and Community Enterprise) Act*⁸⁰⁶ and has the role of the Community Interest Community Regulator (CICR).⁸⁰⁷ The CICR is to provide guidance and assistance to any matter relating to a CIC.⁸⁰⁸ Similar to the Commission, the CICR is to maintain public confidence in CICs.⁸⁰⁹

⁷⁹⁸ *Companies Act 2006* (UK) c 46, s 175(2).

⁷⁹⁹ *Companies Act 2006* (UK) c 46, s 175(3).

⁸⁰⁰ *Companies Act 2006* (UK) c 46, s 175(4).

⁸⁰¹ *Companies Act 2006* (UK) c 46, s 175(6).

⁸⁰² *Companies Act 2006* (UK) c 46, s 181(2)(a).

⁸⁰³ *Companies Act 2006* (UK) c 46, s 181(2)(b).

⁸⁰⁴ *Companies Act 2006* (UK) c 46, s 179.

⁸⁰⁵ *Companies Act 2006* (UK) c 46, s 176(2).

⁸⁰⁶ *2004* (UK) c 27.

⁸⁰⁷ The regulator's office of CICs does not have an official title such as, Companies House. Therefore, this thesis will refer to the regulator of Community Interest Companies as the Community Interest Regulator.

⁸⁰⁸ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 27(5).

⁸⁰⁹ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 41(1).

The CICR can exercise its investigative and supervisory powers in circumstances where it appears there is misconduct, or mismanagement, in the administration of a CIC.⁸¹⁰ Should there be a need to protect a CIC's property, or to secure the proper application of CIC's property, the CICR may order that the property be vested, or transfer the property to the Official Property Holder.⁸¹¹ The CICR may order certain persons not to part with the CIC's property, or make any payments in respect to the debtor's liability. Such an order can be granted without the CICR's consent.⁸¹² Should any person fail to comply with such an order, the CICR may bring civil proceedings against that person⁸¹³ and, with the consent of the Director of Public Prosecutions, instigate a prosecution.⁸¹⁴ The CICR may appoint a manager to oversee the property and affairs of the CIC.⁸¹⁵ The appointed manager can have the same functions as a CIC director, and may be prevented from exercising any of a company director's functions by the CICR.⁸¹⁶ Further, the CICR may discharge an order to appoint a person to be an administrative receiver, administrator, provisional liquidator, or a liquidator of the CIC.⁸¹⁷

Under the CICR's supervisory powers, a director maybe appointed and removed.⁸¹⁸ Appointing a director for the CICR is by order, which details the terms and period for which the director can hold office.⁸¹⁹ An order to suspend a director will only remain in force until the decision to remove the director has been made.⁸²⁰ Where the Regulations permit the distribution of a CIC's assets to members, the CICR may set limits on payment of interest, on debentures, or

⁸¹⁰ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 41(3)(a)-42.

⁸¹¹ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, ss 29, 41(3)(b), 48(1). Vesting or the transfer of property is not a breach of a covenant or condition against alienation and the right of reverter, pre-emption, forfeiture, re-entry, irritancy and option. *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 48(4)-(5).

⁸¹² *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 48(3).

⁸¹³ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 12.

⁸¹⁴ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 48(10).

⁸¹⁵ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 47(1).

⁸¹⁶ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 47(4).

⁸¹⁷ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 47(8).

⁸¹⁸ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, ss 45-46.

⁸¹⁹ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, sub-cl 45(4)-(5).

⁸²⁰ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 46(3). The CICR can only suspend a director for a maximum of twelve months. *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 46(4).

debts issued by the CIC.⁸²¹ A CIC with share capital may be ordered by the CICR to transfer shares and pay dividends to new members.⁸²²

7.2.10 Forward Thinking ...

The parliament of the United Kingdom understood that not-for-profits have evolved into trading, commercial enterprises, and the CIC form liberalises the strict traditional parameters of not-for-profit organisations. Pluralists would reject the form of the CIC, as it could be argued that it detracts from the purity of achieving charitable objectives – but the reality is that the opposite is happening. Not-for-profits engage in trade for non-primary purposes by undertaking business activities – for example, selling goods in a charity gift shop.⁸²³ Rather than discount the CIC form, it has shown that it provides advantages for not-for-profit organisations pursuing a certain social and altruistic activity – which even the pluralist would agree with.

A CIC can be a trading subsidiary to the main charity, and this arrangement provides clear differentiation between the main charitable mission and its financial or trading operation/s.⁸²⁴ The two arms of this hybrid organisation would not detract from the charity's altruistic objectives but, rather, the commercial aspect complements and support the charity's purpose. This innovative form allows an ancillary trading structure to a not-for-profit organisation, and it should be considered in Australia.⁸²⁵

As already noted, many Australian not-for-profit organisations operate commercial ventures that are an extension of the organisation's community purpose.⁸²⁶ Trading not-for-profits in Australia

⁸²¹ *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, s 30.

⁸²² *Companies (Audit, Investigations and Community Enterprise) Act 2004* (UK) c 27, sub-cl 49(1)–(4).

⁸²³ Oonagh Breen, 'Holding the Line: Regulatory Challenges in Ireland and England when Business and Charity Collide' in Myles McGregor-Lowndes and Kerry O'Halloran (eds), *Modernising Charity Law Recent Developments and Future Directions* (Edward Elgar Publishing, 2010) 139.

⁸²⁴ Oonagh Breen, 'Holding the Line: Regulatory Challenges in Ireland and England when Business and Charity Collide' in Myles McGregor-Lowndes and Kerry O'Halloran (eds), *Modernising Charity Law Recent Developments and Future Directions* (Edward Elgar Publishing, 2010) 150-151.

⁸²⁵ Oonagh Breen, 'Holding the Line: Regulatory Challenges in Ireland and England when Business and Charity Collide' in Myles McGregor-Lowndes and Kerry O'Halloran (eds), *Modernising Charity Law Recent Developments and Future Directions* (Edward Elgar Publishing, 2010) 149-151.

⁸²⁶ Five hundred (500) not-for-profit organisations were surveyed and it was found that 29% of these organisations undertook commercial ventures and provided commercial services as part of the organisation's purpose. Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 240.

are referred to as social enterprises,⁸²⁷ and the Productivity Commission took the view that these should create a partnership with government and the for-profit sector.⁸²⁸ However, the Productivity Commission's suggestion was stated with some caution by acknowledging the nature of a not-for-profit organisation provide risks and limited financial returns for investors.⁸²⁹ Discussion on how to improve the commerciality of not-for-profit organisations, or to create a form similar to a CIC, has stalled and the discussion is mainly focused on establishing a national regulator.

7.3 The Regulator for Charities and Other Not-for-Profit Organisations

7.3.1 The Charity Commission

The Commission supervises the not-for-profit forms of charities, charitable incorporated associations, and unincorporated associations and charities in England and Wales. The Commission can best be described as a 'one-stop shop' that offers everything conceivable that a not-for-profit organisation would need.⁸³⁰ The Commission functions as a regulator, an advisor, an educator, and an administrator – not only to charities, but also to the whole of the not-for-profit sector.

7.3.2 Status of the Commission

The Commission forms part of the civil service, a non-ministerial government department.⁸³¹ While it performs its function on behalf of the Crown, it is crucial that the Commission remains independent from any government and/or ministerial influence.⁸³² The significance of the Commission remaining independent is in that it ensures it acts as the sector's guardian to protect

⁸²⁷ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 247.

⁸²⁸ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 247. Chapter Eight of this thesis discusses the partnership between government and the not-for-profit sector.

⁸²⁹ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010) 247.

⁸³⁰ The term 'charity' or 'charities' in the United Kingdom context often encompasses all forms of not-for-profit organisations. For the purpose of this chapter, 'charity' should not be read to exclusively mean a charitable trust.

⁸³¹ Charity Commission, 'Our Status' <http://www.charity-commission.gov.uk/About_us/About_the_Commission/Our_status_index.aspx>.

⁸³² *Charities Act 2006* (UK) c 50, s 1A(3); *Charities Act 2011* (UK) c 25, s 13(3).

it from political interests. However, the strictness of the Commission's independence is questioned given its partnership and close relationship with the government.⁸³³

The Commission's two-way partnership (with the government and the sector) requires it to promote awareness of the sector and represent the sector's concerns to government.⁸³⁴ The Commission is required to annually report to, and respond to any requests from, the Office of Civil Society within the Cabinet Office under the Minister for Civil Society.⁸³⁵

7.3.3 *The Commission's Objectives*

The Commission has five key objectives:

1. *the public confidence objective* – the Commission is to take action that will increase public trust and confidence in charities;⁸³⁶
2. *the public benefit objective* – the Commission is to promote awareness and understanding of the public benefit requirements;
3. *the compliance objective* – the Commission is to promote compliance by charity trustees with their legal obligations in exercising control, management and administration of their charities;
4. *the charitable resources objective* – the Commission is to promote the effective use of charitable resources; and
5. *the accountability objective* – the Commission is to promote the effective use of charitable resources.⁸³⁷

⁸³³ Alison McLennan, *Blackstone's Guide to the Charities Act 2006* (Cambridge University Press, 2007) 17.

⁸³⁴ Hubert Picarda QC is critical of the Commission's two-way relationship with the sector and the government. He argues that government policy concerning the sector often emanates from the Commission, which makes it only the mouthpiece for the sector and, consequently, negatively impacts the sector's independence. Having the Commission speaking on behalf of the sector excludes small not-for-profit organisations from these discussions. Conversely, having the Commission as the trusted expert, not-for-profit organisations rely on the Commission taking control of the issues, and its views may not necessarily reflect the values of some not-for-profit organisations. Hubert Picarda QC, 'Harmonising Nonprofit Law in the EU' in Klaus Hopt and Thomas Von Hippel (eds), *International Corporate Law and Financial Market Regulation – Comparative Corporate Governance of Non-Profit Organisations* (Cambridge University Press, 2010) 182.

⁸³⁵ Prior to the election of the Liberal Democrat Party to government, the Commission's reporting requirements were directly to the Office of the Third Sector. *Charities Act 2006* (UK) c 50, s 7. The Office of the Third Sector has been replaced with the Office of Civil Society. Subsequently, the Commission is to report to the Office of Civil Society, to the Informal Minister on the Big Society and to the Home Affairs' Committee Cabinet. Big Society is the name given for the government's agenda to empower communities to make their own decisions about their local area, open the public service to allow charities, social enterprises, and private companies to compete with each other to offer high quality services, and to encourage social action that allows people to become more active in society. Office of Civil Society, 'Big Society – Overview' <<http://www.cabinet.gov.uk/content/big-society-overview>>; Office of Civil Society, 'Structure' <<http://www.cabinetoffice.gov.uk/resource-library/office-civil-society-structure-finalised>>

⁸³⁶ *Charities Act 2006* (UK) c 50, s 1B(3); *Charities Act 2011* (UK) c 25, s 14.

These overarching objectives are at the centre of how the Commission carries out its general and specific functions.

7.3.4 The Commission's General Functions

The general functions of the Commission are to:

1. make determinations about whether organisations are charities or not;
2. encourage and facilitate better administration of charities;
3. identify and investigate apparent misconduct or mismanagement in the administration of charities, and to take remedial or protective action in connection with misconduct or mismanagement;
4. determine whether or not public collection certificates should be issued and remain in force;
5. obtain, evaluate and disseminate information in connection with the performance of the Commission's functions and its objectives; and
6. give information, advise or make proposals to any Minister of the Crown on matters relating to any of the Commission's functions and how objectives are being satisfied.⁸³⁸

By combining these statutory functions and powers, the Commission is a super-sized statutory body that is all things to the not-for-profit sector. The Commission is a registry, regulator, an educator, and an advisor to the not-for-profit sector and its organisations, and each one of these functions will be individually examined.⁸³⁹

7.3.5 The Commission as a Registry

The Commission is to keep and maintain a register of charities. As the registry of charities, it creates a single point for registration. How this registry is maintained is at the discretion of the Commission.⁸⁴⁰ The information that the Commission makes available to the public for inspections is comprehensive.⁸⁴¹

⁸³⁷ *Charities Act 2006* (UK) c 50, s 1B(3); *Charities Act 2011* (UK) c 25, s 14.

⁸³⁸ *Charities Act 2006* (UK) c 50, s 1C(2); *Charities Act 2011* (UK) c 25, s 15(1)(6).

⁸³⁹ *Charities Act 1993* (UK) c 10, s 9; *Charities Act 2006* (UK) c 50, s 1C(3); *Charities Act 2011* (UK) c 25, s 29.

⁸⁴⁰ *Charities Act 1993* (UK) c 10, s 3(3)(b); *Charities Act 2011* (UK) c 25, s 29(1).

⁸⁴¹ *Charities Act 2006* (UK) c 50, s 3; *Charities Act 2011* (UK) c 25, s 38(1).

Generally, it is thought that every charity must be registered with the Commission. However, there are some forms of charities that are not required to be registered:⁸⁴² (i) excepted; and (ii) exempt charities.

7.3.6 *Excepted Charity*

Despite this specific form of organisation falling outside the need to be registered, an excepted charity does remain under the supervision of the Commission.⁸⁴³ Examples of an excepted charity are those connected with churches and chapels belonging to a Christian denomination, charitable services of the armed forces, or scouts and guide groups.⁸⁴⁴ However, excepted charities with an annual income over £100,000 must be registered with the Commission, unless the Commission issues the excepted charity status with a written determination to the contrary.⁸⁴⁵ The Commission also has the power to order a charity to be exempted from registration on a permanent, or temporary basis.⁸⁴⁶

7.3.7 *Exempted Charity*

An exempt charity is exempted from registering with the Commission and, generally, this form of charity is not under the Commission's supervision. However, the Commission, being all things to charities, can provide support to exempt charities.⁸⁴⁷ An organisation that is an exempt charity must be listed in Schedule 2 of the 1993 *Charities Act*.⁸⁴⁸ Any small charity with a gross annual income less than £5,000 is considered an exempt charity and, therefore, does not need to be

⁸⁴² Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 28; *Charities Act 2006* (UK) c 50, s 3A; *Charities Act 2011* (UK) c 25, s 30(2).

⁸⁴³ Full supervision by the Commission means that an excepted charity must provide information about its activities. The Commission has the power to investigate the excepted charity if there is a cause of concern. Charity Commission, 'Changes to the Regulation of Excepted and Exempt Charities' (July 2010) <http://www.charity-commission.gov.uk/Start_up_charity/Do_I_need_to_register/regreq.aspx> 2.

⁸⁴⁴ Charity Commission, 'Changes to the Regulation of Excepted and Exempt Charities' (July 2010) <http://www.charity-commission.gov.uk/Start_up_charity/Do_I_need_to_register/regreq.aspx> 2.

⁸⁴⁵ *Charities Act 2006* (UK) c 50, s 3A(2)(b)-(c)(ii); *Charities Act 2011* (UK) c 25, s 30.

⁸⁴⁶ *Charities Act 2006* (UK) c 50, s 3A(2)(b)(i); *Charities Act 2011* (UK) c 25, s 32(b)

⁸⁴⁷ An exempt charity may seek an order from the Commission that enables it to take action where its governing document does not allow it to undertake such action. Charity Commission, 'Changes to the Regulation of Excepted and Exempt Charities' (July 2010) <http://www.charity-commission.gov.uk/Start_up_charity/Do_I_need_to_register/regreq.aspx> 3.

⁸⁴⁸ Examples of exempt charities listed in Schedule 2 are the universities of Oxford, Cambridge, Durham and Newcastle, Queen Mary and Westfield College in the University of London, and the colleges of Winchester and Eton. For further exempt charities, refer to Schedule 2 *Charities Act 1993* (UK) c 10 and Schedule 3 of the *Charities Act 2011* (UK) c 25.

registered.⁸⁴⁹ However, small charities still have access to the support, advice and resources of the Commission.

7.3.8 *Removal of a Charity from the Registry*

Despite clear statutory provisions requiring a charity to be registered, the decision of registration ultimately lies within the Commission's discretionary power. The Commission also has the discretionary power to remove a charity from the registry.⁸⁵⁰ Removal of a charity from a registry occurs when the Commission regards the charity to no longer be a charity and/or it has ceased to exist or be in operation.⁸⁵¹ The removal of institutions from the registry (including cancelled institutions) is available for public inspection.⁸⁵²

7.3.9 *The Commission as an Investigator*

Before the Commission can make any order relating to the operation of a charity, it has numerous powers to undertake inquiries.⁸⁵³ The Commission and its staff have the power to enter a charity's premises and seize its documents during an investigation.⁸⁵⁴ Entering a charity's premises is limited, and a warrant must be obtained from a Justice of the Peace. For the Justice of the Peace to grant a warrant, the Commission must evidence the following:

1. that an inquiry has been instituted by the Commission;
2. there is reason to believe that without a warrant the trustee would refuse to produce the document; or
3. there are grounds for belief that documents, or information will be destroyed if not seized.

Under the *Criminal Justice and Police Act 2001* (UK), the Commission has a conferred power to seize material for the purpose of an inquiry.⁸⁵⁵ Should the Commission be intentionally obstructed

⁸⁴⁹ *Charities Act 2006* (UK) c 50, s 3A(2)(c), sch 2; *Charities Act 2011* (UK) c 25, s 22, sch 3.

⁸⁵⁰ *Charities Act 1993* (UK) c 10, s 3(4); *Charities Act 2011* (UK) c 25, s 34.

⁸⁵¹ *Charities Act 2006* (UK) c 50, s 3(4)(b); *Charities Act 2011* (UK) c 25, s 34(1)(a)-(b).

⁸⁵² *Charities Act 2006* (UK) c 50, s 3(7); *Charities Act 2011* (UK) c 25, s 34.

⁸⁵³ *Charities Act 1993* (UK) c 10, s 8; *Charities Act 2011* (UK) c 25, s 46.

⁸⁵⁴ *Charities Act 1993* (UK) s 31A; *Charities Act 2006* (UK) c 50, s 26; *Charities Act 2011* (UK) c 25, s 56A.

⁸⁵⁵ *Criminal Justice and Police Act 2001* (UK) c 16 pt 1, sch1.

by anyone during a search, this will constitute a summary offence and the offender will be punished.⁸⁵⁶

7.3.10 The Commission as a Regulator

The Commission has the statutory power to regulate charities of all sizes and descriptions.⁸⁵⁷ Its primary role as a regulator is to monitor and control charities by ensuring:

- compliance with charity law;
- that abuses and poor practices are dealt with;
- that charities work better within an effective legal, accounting and governance framework; and
- the promotion of sound governance and accountability.⁸⁵⁸

The Commission, in carrying out this function and to meet its legislative objectives, has the following regulatory powers:

- a) suspending or removing trustees and members;
- b) making directions to protect a charity;
- c) directing the application of charity property;
- d) ordering administration schemes;
- e) determining a charity's membership; and
- f) restricting a charity's mortgage.

Each one of these powers and the circumstances in which the Commission may rely upon these powers is examined individually.

7.3.10.1 Power to Suspend or Remove Trustee

The Commission is permitted to suspend or remove any trustee, officer, agent or employee.⁸⁵⁹ Where a trustee, an officer, agent or employee has membership of a

⁸⁵⁶ Punishment may be a fine not exceeding level 5 on the standard scale; imprisonment up to 51 weeks; or both. *Charities Act 2006* (UK) c 50, s 26(11); *Charities Act 2011* (UK) c 25, s 49(8).

⁸⁵⁷ *Charities Act 2006* (UK) c 50, s 1(4)(c), sch 1A; *Charities Act 2011* (UK) c 25, ss 25-26.

⁸⁵⁸ Charity Commission, 'The Charity Commission and Regulation' (January 2010) <http://www.charity-commission.gov.uk/Our_regulatory_activity/Our_approache/regstance.aspx#1> 2.

⁸⁵⁹ *Charities Act 2006* (UK) c 50, s 18A; *Charities Act 2011* (UK) c 25, s 82-83. A trustee's suspension is for one year and the Commission is obliged to review a suspension order. The Commission may discharge a suspension order, if appropriate. *Charities Act 1993* (UK) c 50, s 18A; *Charities Act 2011* (UK) c 25, s 83.

charity, the Commission may order the termination of the individual's membership,⁸⁶⁰ or order an expelled member to be prohibited from resuming membership of that charity.⁸⁶¹ This specific power, of removing or suspending a trustee from office or employment, is not unfettered, and the Commission will use this power in two particular scenarios. The first occurs when the Commission is satisfied that there has been misconduct, mismanagement, or someone was privy to the misconduct in the administration of the charity.⁸⁶² The second is when the Commission decides it is necessary to protect the charity, its purpose, its property, or to secure the proper application of the charity's property or property coming to the charity.⁸⁶³

The action that the Commission may take in removing or suspending a trustee might result in a charity ceasing operation. Forcing a charity to cease would have a negative impact for volunteers and individuals who rely upon on the delivery of a charity's services. An alternative to this strong-handed approach is for the Commission to use its remedial powers to order a charity to continue operating when the Commission is considering removing or suspending a trustee.⁸⁶⁴ The Commission may, during this time, appoint additional trustees and vest a charity's property to be held on trust by an official custodian.⁸⁶⁵ Furthermore, the Commission may appoint an interim manager and a receiver regarding the charity's property and its affairs.⁸⁶⁶

⁸⁶⁰ *Charities Act 2006* (UK) c 50, s 18A(1)(b); *Charities Act 2011* (UK) c 25, s 83.

⁸⁶¹ *Charities Act 2006* (UK) c 50, s 18A(1)(b); *Charities Act 2011* (UK) c 25, s 83(4). The resumption of membership is permissible after five years of suspension only with consent by the Commission. *Charities Act 2006* (UK) c 50, s 18A(4); *Charities Act 2011* (UK) c 25, s 83(5).

⁸⁶² Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 34.

⁸⁶³ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 34.

⁸⁶⁴ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 34.

⁸⁶⁵ *Charities Act 1993* (UK) c 10, s 21-22; *Charities Act 2011* (UK) c 25, s 76. The official custodian merely holds the property on behalf of the charity and does not exercise any functions of a trustee regarding the management and control of the charity. Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) n 21, 34. Once the Commission has ordered the transfer of property to the official custodian, then trustees are not to deal with the property or monies without prior consent from the Commission. Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 34.

⁸⁶⁶ Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 34.

7.3.10.2 *Power to Give Specific Directions for the Protection of Charity*

Where the Commission is satisfied that there has been misconduct or mismanagement, an order can be made to certain persons to act appropriately.⁸⁶⁷ This power allows the Commission the option to appoint a receiver, another trustee or a manager to take the action that the Commission thinks is necessary to protect the charity and to avoid it ceasing operation.

Whatever the Commission's directions, they must not be inconsistent with any Act of Parliament,⁸⁶⁸ or be inconsistent with the charity's purpose.⁸⁶⁹ Once the Commission provides direction for action, the person directed must act expediently and in the interests of the charity.⁸⁷⁰

7.3.10.3 *Power to Direct Application of Charity Property*

Where a person is in control of, or in possession of, any property held in trust for a charity and are unwilling to apply it properly for the purpose of the charity, the Commission will take action.⁸⁷¹ The Commission can order the relevant person to apply the charity's property in a manner that the Commission states.⁸⁷² Unwillingness by a trustee to apply the charity's property properly does not infer that there has been any misconduct, dishonesty, bad faith or mismanagement.⁸⁷³ The Commission will intervene where it is satisfied that not only a trustee is unwilling to act properly, but also to secure the proper application of property for the charity's purpose.⁸⁷⁴

Additionally, the Commission can appoint a receiver or manager where a charity lacks the power to act in a way the Commission has directed the trustee. This often occurs when charities have an older constitutional document that lacks the power for a

⁸⁶⁷ *Charities Act 1993* (UK) c 10, s 19A; *Charities Act 2006* (UK) c 50, s 20; *Charities Act 2011* (UK) c 25, s 84. A person whom the Commission can direct is: any trustee; any officer; any employee; and the charity itself (if the charity is a body corporate). *Charities Act 1993* (UK) c 10, s 19A(2); *Charities Act 2011* (UK) c 25, s 82-83.

⁸⁶⁸ Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 35.

⁸⁶⁹ *Charities Act 1993* (UK) c 10, s 19A(3); *Charities Act 2011* (UK) c 25, s 84(3)(b).

⁸⁷⁰ *Charities Act 1993* (UK) c 10, s 19A; *Charities Act 2011* (UK) c 25, s 48(4).

⁸⁷¹ *Charities Act 1993* (UK) c 10, s 19B(1); *Charities Act 2011* (UK) c 25, s 85(1).

⁸⁷² *Charities Act 1993* (UK) c 10, s 19B(2); *Charities 2011* (UK) c 25, s 85(1)(b).

⁸⁷³ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 36.

⁸⁷⁴ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 35.

trustee to act in the manner directed.⁸⁷⁵ An older constitutional document may restrict a trustee from disposing certain types of land or to transfer land.⁸⁷⁶

7.3.10.4 *Ordering Administrative Schemes*

The Commission has concurrent jurisdiction with the High Court for making schemes in relation to the administration of a charity.⁸⁷⁷ A scheme is likely to be directed where there has been a misapplication of funds, or there are other reasons that demand better regulation.⁸⁷⁸

The Commission can devise an administrative scheme to allow the administration of more than one charity under the one scheme.⁸⁷⁹ The scheme also allows for the merger of smaller charities, or where charities of similar nature can become one administrative scheme. The Commission has the power to exercise a property *cy-près* scheme.⁸⁸⁰ For example, in the 1999 case of *Versani v Jesani*, the Commission relied on its power to order a *cy-près* scheme.⁸⁸¹ In *Versani*, there were a number of different charity groups that no longer worshiped together, and the Commission devised a scheme to divide the funds between the two partitioned charity groups.⁸⁸²

7.3.10.5 *Determination of Membership*

The Commission may determine who are members of a charity.⁸⁸³ It relies upon this power when there are internal disputes between the charity's trustees that may be damaging a charity.⁸⁸⁴ To settle an internal dispute, the Commission will appoint a person with authority to restore the charity to a functioning body. This authorised person can: (i) determine the qualification for membership; (ii) sign the constitution or rules of

⁸⁷⁵ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 35.

⁸⁷⁶ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 35.

⁸⁷⁷ *Charities Act 1993* (UK) c 10, ss 16, 19B(3)(b); *Charities Act 2011* (UK) c 25, s 78(6) .

⁸⁷⁸ *Attorney General v Dedham School* (1857) 23 Beav 350.

⁸⁷⁹ *Charities Act 2006* (UK) c 50, s 44; *Charities Act 2011* (UK) c 25, s 73.

⁸⁸⁰ *Charities Act 1993* (UK) c 10, s 14B; *Charities Act 2011* (UK) c 25, s 67(1).

⁸⁸¹ [1999] Ch 219.

⁸⁸² *Versani v Jesani* [1999] Ch 219.

⁸⁸³ *Charities Act 1993* (UK) c 10, s 29A; *Charities Act 2011* (UK) c 25, s 111.

⁸⁸⁴ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 39.

the charity; (iii) make an agreement to abide by those rules; (iv) conduct elections; and (v) do whatever else that is needed to restore the function of the charity.⁸⁸⁵

7.3.10.6 *Restrictions on Mortgaging*

Trustees have the freedom to mortgage the charity's land as security for a loan.⁸⁸⁶ When making arrangements for a mortgage, a charity must have a written advice from a financial expert.⁸⁸⁷ The financial advice sought should address the necessity of the mortgage, if the mortgage's terms are reasonable, and the charity's ability to repay the mortgage.⁸⁸⁸ Where a charity has not sought proper financial advice, then the Commission must give consent to the charity to use their land as security.⁸⁸⁹

Additionally, consent from the Commission is needed by a trustee to extend grants⁸⁹⁰ or loans⁸⁹¹ where the charity's property was used as security.⁸⁹² This power gives the Commission controlling and regulating authority to protect charities from mismanagement.

7.3.11 *Regulation of Exempt Charities*

As noted earlier, exempt charities are not under the supervision of the Commission, which now holds power to regulate exempt charities and to institute inquiries into an exempt charity.⁸⁹³ Additionally, it is permissible for the Commission to make a range of orders to protect an exempt charity,⁸⁹⁴ access a charity's dormant bank accounts, repay monies and disqualify a person.⁸⁹⁵

⁸⁸⁵ *Charities Act 1993* (UK) c 10, s 29A; *Charities Act 2011* (UK) c 25, s 111(3).

⁸⁸⁶ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 41.

⁸⁸⁷ Financial advice must be from an independent person who has no financial interest in providing that advice. A finance officer must be suitably qualified to provide a charity such advice. Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 41.

⁸⁸⁸ Alison MacLennan, *Blackstone's Guide to The Charities Act 2006* (Oxford University Press, 2007) 41.

⁸⁸⁹ *Charities Act 2006* (UK) c 50, s 28; *Charities Act 2011* (UK) c 25, s 124.

⁸⁹⁰ The grant funding can be secured by a charge over the charity's land. Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 41.

⁸⁹¹ Charities have entered into all-money mortgage have experienced problems owing to poor advice, which did not include being informed of all the situations which the charge covered. Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 41.

⁸⁹² *Charities Act 2006* (UK) c 50, s 38; *Charities Act 2011* (UK) c 25, s 124.

⁸⁹³ *Charities Act 2006* (UK) c 50, sch 5, para 4; *Charities Act 2011* (UK) c 25, sch 9 para 7.

⁸⁹⁴ *Charities Act 1993* (UK) c 10, s 18; *Charities Act 2001* (UK) c 25, sch 9, para 18.

⁸⁹⁵ *Charities Act 1993* (UK) c 10, s 28; *Charities Act 2006* (UK) c 50, sch 5, para 7; *Charities Act 2011* (UK) c 25, sch 9, para 20, 25.

7.3.12 The Commission's Proportionality Framework

Carrying out its regulatory function, the Commission follows the principles of best regulatory practice.⁸⁹⁶

- *Proportionate* – The Commission's regulatory action is directed to where there are greater risks to public trust and confidence in a charity.⁸⁹⁷
- *Accountable* – Being accountable to parliament regarding the effective use of the Commission's resources, and providing reasons behind the Commission's decisions to affected individual/s and charity.⁸⁹⁸
- *Consistent* – The Commission will apply the same approach in assessing the risk in every case and decide on an appropriate response to each set of circumstances.⁸⁹⁹
- *Transparent* – The Commission is to be clear about its expectations on how charities operate. The Commission will publish guides, key policies, and regulatory decisions on their website for charities and members of the public to access.⁹⁰⁰
- *Targeted* – Means that any action undertaken by the Commission is directed at cases that possess the greater risks and where the Commission's actions would have an impact when they do act. This also includes the Commission working collaboratively with other regulators and agencies.⁹⁰¹

These principles provide the framework for the Commission to be a risk-based and proportionate regulator. When assessing risk, the Commission states that they are proactive and focused upon preventing problems rather than being reactive.⁹⁰² Where there is an assessment of a serious case,

⁸⁹⁶ Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> 5.

⁸⁹⁷ Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> Annex B, 21.

⁸⁹⁸ Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> Annex B, 21.

⁸⁹⁹ Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> Annex B, 22.

⁹⁰⁰ Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> Annex B, 22.

⁹⁰¹ Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> Annex B, 22.

⁹⁰² Cases which are considered high risk involve: significant financial loss to a charity; serious harm to beneficiaries; using a charity for terrorist purposes; serious criminal and/or illegal activity within or involving a charity; a charity established for illegal or improper purposes; charities used for a private advantage; the charity's independence is questionable; significant non-compliance and breaches of trust or abuse that significantly impact on the public trust and confidence in the charity and the sector. Charity Commission, 'Risk Framework – Application of the Charity Commission's Risk Framework' (January 2012) <www.charitycommission.gov.auk/Library/arf.pdf> 7; Charity Commission, 'Risk Framework – Our Regulatory

the Commission will undertake meaningful investigations and, often, it is required intervene.⁹⁰³ However, the Commission advises that troubles within charities are capable of being resolved early by providing advice and educating the sector and the public.⁹⁰⁴

The Commission's priorities and resources are dedicated to addressing high-risk incidences, but the Commission understands that low-risk problems can damage public trust and confidence in a charity if not dealt with appropriately.⁹⁰⁵

7.3.13 The Commission as an Educator and Advisor

Another important feature of the Commission is to provide the necessary support to charities, and it has the general power to advise trustees.⁹⁰⁶ Advice or guidance provided by the Commission relate to trustees' performance of their legal duties, and other matters relating to the proper administration of the charity. Further, the Commission can issue advice or guidance that is directed at charities in general, at a particular charity, or at any class of charity.⁹⁰⁷ In issuing advice or guidance, the Commission does not need to wait for a written application by an aggrieved person – it can act on its own motion.

The Commission, as an educator, publishes a wide range of information on all topics relating to the administration of charities, which are easily accessible by the Internet.⁹⁰⁸ The Commission also holds a number of events and seminars at various times through the year across England and Wales. These seminar series are part of the Commission's general commitment to promoting the not-for-profit sector, and to increase the public and a trustee's understanding of the operation, administration and legal requirements of a charity.

Approach to Protecting the Public's Interest in Charity – How we Assess and Manage Risks' (January 2012) <www.charitycommission.gov.uk/Library_framework.pdf> 3.

⁹⁰³ Charity Commission, 'Charities Back on Track – Themes and lessons from the Charity Commission's Investigations and Regulatory Casework 2010–11' <www.charitycommission.gov.uk> 4.

⁹⁰⁴ Charity Commission, 'Charities Back on Track – Themes and lessons from the Charity Commission's Investigations and Regulatory Casework 2010–11' <www.charitycommission.gov.uk> 3.

⁹⁰⁵ Charity Commission, 'Charities Back on Track – Themes and lessons from the Charity Commission's Investigations and Regulatory Casework 2010–11' <www.charitycommission.gov.uk> 13.

⁹⁰⁶ *Charities Act 1993* (UK) c 10, s 29; *Charities Act 2011* (UK) c 25, s 15(1)(6), (2).

⁹⁰⁷ *Charities Act 1993* (UK) c 10, s 29; *Charities Act 2006* (UK) c 50, s 1C; *Charities Act 2011* (UK) c 25, s 15(3)

⁹⁰⁸ To see the list of Charity Commission published material go to: <http://www.charity-commission.gov.uk/Charity_requirements_guidance/ccpubs3.aspx>.

7.3.14 Appeal Mechanisms

All decisions of the Commission are not absolute and are subject to review and appeal. The Charity Tribunal (referred to as the ‘First-Tier Tribunal’) was established to hear appeals against, and review decisions of, the Commission.⁹⁰⁹ The First-Tier Tribunal also considers references from the Attorney General or the Commission regarding points of law.

Applications for reviewable matters and appeals are dealt with the First-Tier Tribunal in accordance with Schedule 1C of the 1993 *Act*.⁹¹⁰ Hearing appeals and applications for review, the First-Tier Tribunal has the power to make the following orders:

1. to quash the Commission’s decision;
2. to remit the matter back to the Commission;
3. to submit all or part of the Commission’s order;
4. to add to the Commission’s order (anything that the Commission should have made); and
5. to direct the Commission to rectify their decision.⁹¹¹

Schedule 1C also outlines the person who has *locus standi* to appeal and who can make an application for review to the First-Tier Tribunal. Persons capable of making an application to the First-Tier Tribunal are: the Attorney-General;⁹¹² charity trustees; any persons in control, or management of an organisation; any aggrieved person who has been removed, suspended, or disqualified by an order of the Commission; any person that was affected by the decision made by the organisation; a solicitor; the charity itself; companies; any person affected by the Commission’s decision; and creditors.⁹¹³

⁹⁰⁹ *Charities Act 1993* (UK) c 10, pt 1A, s 2A(4); *Charities Act 2011* (UK) c 25, s 315.

⁹¹⁰ Reviewable matters relates to: (i) the Commission instituting an inquiry into a particular charity; (ii) the Commission inquiring into a class of charities; (iii) the Commission’s refusal to make a common investment scheme; (iv) the Commission not to make a common deposit scheme; and (v) refusal by the Commission to make an order for the disposition of land and allowing a trustee to take a mortgage, or secure a charge of charity land. *Charities Act 2011* (UK) c 25, s 322.

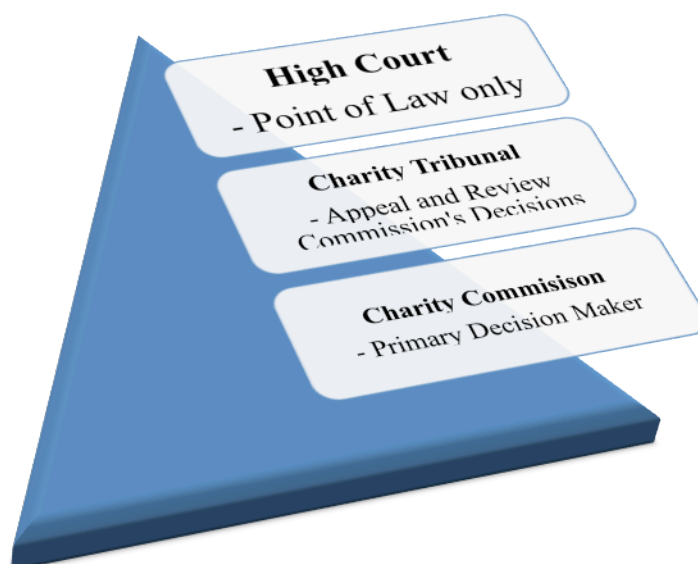
⁹¹¹ Appeals may be brought to the first-tier tribunal against any decision, order and direction of the Commission if listed in the charities legislation. These lists are extensive and prescriptive. *Charities Act 1993* (UK) c 10, col 1, sch 1C; *Charities Act 2011* (UK) c 25, cols 1,2 sch 6.

⁹¹² *Charities Act 1993* (UK) c10, sch 1C, paras 1(2), 3-4; *Charities Act 2011* (UK) c 25, s 362.

⁹¹³ *Charities Act 1993* (UK) c 10, col 2, sch 1C.

Appeals of the First-Tier Tribunal's decisions are made to the High Court,⁹¹⁴ and are confined to point/s of law.⁹¹⁵ Figure 4 provides an overview of the Appeals and Review Structure for Charities.

Figure 4 – Overview of the appeal structure



7.4 Conclusion

Despite all the efforts our federal policy-makers are taking to reform and regulate the not-for-profit sector, their plans are well short of world's best practice. All our policy makers have failed to understand the sector. In an effort to preserve the self-regulatory nature of the not-for-profit sector, the federal government's proposal for reform is disconnected from the public's demand for organisational transparency, and to modernise the sector to best assist organisations to efficiently achieve their mission in a demanding contemporary context. This is something the United Kingdom understood very well.

The first step to modernise the not-for-profit sector in the United Kingdom was to expand the traditional charitable purpose and provide clarity as to whether or not an organisation holds charitable status. Furthermore, the United Kingdom has embraced new forms of organisation, such as the Charitable Incorporated Organisation and the Charitable Unincorporated Association.

⁹¹⁴ *Charities Act 1993* (UK) c 10, s 2C(1); *Charities Act 2011* (UK) c 25, s 321(2) col 2, sch 6.

⁹¹⁵ *Charities Act 1993* (UK) c 10, s 2C(2); *Charities Act 2011* (UK) c 25, 321(4)

These engage in commercial revenue raising exercises, such as attracting investors rather than attracting a donor.

Further, the United Kingdom emphasises that trustees and directors have responsibilities and legal duties to the organisation. The Commission in overseeing the not-for-profit sector must ensure that the management of any not-for-profit organisation is carried out in a manner that will not compromise confidence in the sector and its organisations.

To achieve confidence in the sector, the Commission has been designed to be all things to the sector. It is not only the sector's guardian, but also its mouthpiece and, regardless of Picarda's QC concerns about the Commission's independence, its centralised position brings about necessary change that will benefit and sustain the sector into the future. Therefore, it would be better to have the Commission occupying this position, to advocate through a single voice, than having nothing at all – which is the situation in Australia.

The Commission preserves and ensures that confidence in the sector is not compromised. It would advise, educate, and regulate the sector and its organisations. In providing advice and education to charities, it offers a necessary and timely guidance for a charity to operate in delivering important services, which the public can confidently rely on. Ensuring proper management and transparency within a charity, the Commission has wide regulatory powers to remove, suspend, and disqualify a trustee and/or a member. When exercising its regulatory powers, the Commission will do so proportionately and, moreover, it will work with a charity. Therefore, it is clear that the United Kingdom's Charity Commission represents world's best practice.

CHAPTER 8: The Reform Picture so far ...

*'It is through not-for-profit organisations that government and communities are able to work together to support and strength our democracy.'*⁹¹⁶

8.0 Introduction

Reform of Australia's not-for-profit sector has been long overdue. There has been an array of opinions and recommendations generated from numerous reports and inquiries provided to the federal government, with many options on how to best reform the sector. The centrepiece of the federal government's reform is the Australian Charities and Not-for-Profits Commission. This chapter outlines what entities qualify for registration with the Australian Charities and Not-for-Profits Commission and, furthermore, the structure, function, and regulatory and enforcement powers of the Commission will be analysed. Furthermore, the Commission's enforcement powers are discretionary, and this chapter analyses these powers and other discretionary powers it has.

8.1 The Reform Picture so far

Reforming the not-for-profit sector has been sporadic and slow, and more than a decade after the first parliamentary inquiry into charities, the federal government has made some advances towards reform. Active reform can be seen to have occurred in the areas of taxation, fundraising, financial reporting, and regulation with the establishment of a statutory regulator called the Australian Charities and Not-for-Profit Commission.⁹¹⁷

8.2 The Australian Charities and Not-for-Profit Commission

The centrepiece of the federal government's reform is the new Australian Charities and Not-for-Profits Commission (the ACNC). The ACNC is promised to be a specialist regulator for the

⁹¹⁶ Australian Government, *National Compact: Working Together* (2011) Foreword, 3.

⁹¹⁷ The federal government has amended the income taxation law to improve public ancillary funds, and expand deductible gift receipt status to fire brigades and other state recognised emergency services. See *Tax Laws Amendment Bill 2011*.

sector committed to delivering best practice regulation.⁹¹⁸ For the first time in Australia we have a dedicated body with the responsibility and regulatory authority specifically for not-for-profit organisations; but to understand the ACNC, an examination of its design and scope is needed.

8.3 The Structure and Functions of the ACNC

8.3.1 ACNC's Structure

The organisational structure of the ACNC is simple and is made up of an advisory board, a Commissioner, and staff who assist the Commissioner.⁹¹⁹ The role of the Commissioner is central to the administration of this regulatory framework, which is aimed at enhancing the public's trust and confidence in the sector.⁹²⁰ To achieve these fundamental objectives, the Commissioner has been given prescribed statutory functions.

8.3.2 ACNC's Functions

The ACNC will have two general functions: to register not-for-profit entities; and to monitor them – each of these general functions will be individually examined.⁹²¹

8.3.3 Registering Not-for-Profit Entities

In implementing the Productivity Commission's recommendation, the Commissioner's main role will be to register certain entities. The Commissioner will have the power to register a not-for-profit entity satisfying the following conditions:

⁹¹⁸ Susan Woodward and Andrea Fung, 'In Recognition of their Importance – A Specialist Regulator for Australian Charities' (July 2012) <http://acnctaskforce.treasury.gov.au/content/Content.aspx?doc=publications/articles/NFP_specialist_regulator_July2012/index.htm>.

⁹¹⁹ *ACNC Bill* div 105 cl 105-10; *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 135–15.

⁹²⁰ *ACNC Bill* pt 1–2 dv 15 cl 15–5(1); *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s15–10(a).

⁹²¹ The federal government's 2011 budget outlined several functions of the ACNC not found in the *ACNC Bill*. For example, the 2011 budget stated that the ACNC will have the function of educating and supporting the not-for-profit sector; however, pursuant to the *ACNC Bill* and *Act*, it will only provide education and guidance to those entities registered with the ACNC (see 8.3.3 of this thesis for an description of the type of entities that may register with the ACNC). See also Australian Government Budget 2011–12, Budget Paper No.2 – Part 2: Expense Measures <http://www.budget.gov.au/2011-12/content/bp2/html/bp2_expens-22.htm> 4; *ACNC Bill* dv 15 cl 15-10(g); *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 15–10(g).

- has an Australian Business Number (ABN);⁹²²
- is not a terrorist entity, a criminal entity, or an outlawed entity;⁹²³
- complies with governance standards and external conduct standards;⁹²⁴ and
- to remove any doubt an entity is the type or a subtype of entity.⁹²⁵

Registration with the ACNC is a prerequisite for organisations to access Commonwealth tax concessions and other government exemptions, benefits and concessions.⁹²⁶ Previously, the ATO determined an organisation's charitable status; but now, this decision is made by the ACNC.⁹²⁷ The role of the ATO is confined to administering a not-for-profit organisation's tax status.⁹²⁸

8.3.4 *What is a not-for-profit entity for the purpose of registration?*

Pursuant to the *Australian Charities and Not-for-Profit Commission Act 2012* (Cth), a responsible entity means the following:⁹²⁹

- an individual;⁹³⁰
- a body corporate;⁹³¹
- a body politic;⁹³²
- a constitutional corporation;⁹³³
- an unincorporated association, or a body of persons;⁹³⁴
- a trust;⁹³⁵ or

⁹²² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 25-5(3)(c).

⁹²³ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 25-5(3)(d).

⁹²⁴ The *ACNC Bill* states that the regulations will specify governance and external conduct standards. *ACNC Bill* ch 3 pt 3-1 dv 45 cl 45-10-50-10. At the time of writing this thesis, the regulations were not available. Furthermore, section 50-15 of the *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) states that before regulations can be made, the Governor-General must be satisfied that appropriate level of consultation be undertaken. See *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 50-15(1)(a)(i)–(iv).

⁹²⁵ *ACNC Bill* ch 2 pt 2 dv 25 cl 25-5 (3); *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 25-5(2).

⁹²⁶ *ACNC Bill* ch 2 pt 2-1 dv 20 cl 20-5; *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 20-5.

⁹²⁷ *ACNC Bill* ch 2 pt 2-1 dv 25 cl 20-5; *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 30-10.

⁹²⁸ Federal Treasurer, 'Budget, Budget Measures, Budget Number 2 2011-12, 322. 10 May 2012.

⁹²⁹ Hereafter referred to as the *ACNC Act*.

⁹³⁰ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-5(1)(a).

⁹³¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-5(1)(b).

⁹³² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-5(1)(c).

⁹³³ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-15.

⁹³⁴ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-5(1)(e).

⁹³⁵ The *ACNC Act* notes that a trust is not a legal person and therefore a trustee of a trust is taken to be an entity. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-5(e).

- a not-for-profit entity.⁹³⁶

The *ACNC Bill* provided that a not-for-profit entity was a type of entity that qualified for registration with the ACNC.⁹³⁷ However, the *ACNC Bill* did not expressly provide a meaning of a not-for-profit entity, but makes reference to the *Income Tax Assessment Act 1997* (Cth).⁹³⁸ The glitch here is that this *Act* does not provide a definition of a not-for-profit entity – it is the preceding *Income Tax Assessment Act 1986* (Cth) that defines a not-for-profit entity. Section 3 of the 1986 *Act* defines a not-for-profit entity to be a company that does not carry on for the purpose of profit or gain to its individual members, and where the terms of the its constitution prohibits any distribution of money or property to its members or a friendly society dispensary. This definition may be sound for taxation purposes, but it fails to capsulate all of the structural operational characteristics of a not-for-profit entity. However, the *ACNC Act* does not provide the meaning of a ‘not-for-profit entity’, which is a mystery – therefore, the *Bill* is the guiding instrument. The *ACNC Act* attempts to remedy this shortfall by offering another type of entity that qualifies for registration with the ACNC, which is simply referred to as a ‘type of entity’ and a ‘subtype of entity and also a registered entity.’⁹³⁹ Essentially, a registered entity is a charity, as outlined in Table 8.

Table 8 – Description of an entity and a subtype of entity⁹⁴⁰

Type of Entity	Subtype of Entity
Charity	Entity with a purpose that is the relief of poverty, sickness or the needs of the aged.
	Entity with a purpose that is the advancement of education.
	Entity with a purpose that is the advancement of religion.
	Entity with another purpose that is beneficial to the community.
	Institution whose principal activity is to promote the prevention or the control of disease in human beings. This also includes institutions whose principal activity is to promote the prevention or the control of diseases in human beings.
	Public benevolent institution.
	Entity with a charitable purpose described in section 4 of the <i>Extensions of Charitable Purpose Act 2004</i> (Cth) (provision of child care services).

⁹³⁶ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 25-5(3)(a).

⁹³⁷ *ACNC Bill* ch 8 pt 8-1 dv 205-5 sub dv 205-A cl 205-5(1).

⁹³⁸ *ACNC Bill* ch 8 pt 8-2 dv 900 cl 900-5.

⁹³⁹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 25-5.

⁹⁴⁰ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 25-5(5).

The above description of a registered entity is a direct reflection of the traditional charitable purposes and, unfortunately, the *ACNC Act* offers no advancement or modernisation of the traditional charitable purposes. Once the Commissioner has made a determination to register a registered entity and a responsible entity, the ACNC then moves into a position to monitor it.

8.3.5 *The Monitoring Function of the ACNC*

The monitoring of these entities is achieved through financial reports submitted to the ACNC.⁹⁴¹ The *ACNC Act* provides that an entity must submit once a year an annual information statement to the ACNC that annexes an entity's financial report.⁹⁴² Precisely what information an entity is obliged to record in an annual information statement is not detailed in the *ACNC Bill*, the *ACNC Act* or in its Explanatory Material – however, an entity's financial report must correctly record and explain its transactions, financial position, and performance that is capable of being audited.⁹⁴³ However, these reporting requirements are only applicable to large- and medium-sized entities; small and basic religious entities are excluded from this requirement.⁹⁴⁴ Table 9 provides a description of what constitutes a small, medium and large entity.

⁹⁴¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-5. Although the ACNC Act provides an ACNC officer with statutory powers to enter premises under a monitoring warrant. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) ss 75-15 – 75-20. An entity will be subject to monitoring if non-compliance with the ACNC Act and any provision of the *Crimes Act 1914* (Cth). *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-3.

⁹⁴² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-5. An entity must provide the ACNC with an annual information statement before 31 December in the following financial year. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-5(2)- 60-10(2). However, an entity with the permission of the Commissioner may defer the submission of an entity's annual information statement. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-5(2). Furthermore, the Commissioner may approve a different accounting period. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-85.

⁹⁴³ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-15. Only medium and large registered entities are required to have annual reports audited or reviewed. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) ss 60-20-60-25.

⁹⁴⁴ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 60-10. A basic religious charity is a registered entity as a subtype of entity (the purpose of advancing religion), which is outlined, in the second column of Table 10 above. However, if an entity is registered under the *Corporations Act 2001*(Cth), the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) and the incorporated association legislation of the states and territories the entity is not a basic religious charity.

Table 9 – Description of a small, medium and large entity⁹⁴⁵

Size of Entity	Qualification
Small	Revenue for a financial year is less than \$250,000. ⁹⁴⁶
Medium	Revenue for a financial year is less than \$1,000,00. ⁹⁴⁷
Large	Not a small or a medium registered entity. ⁹⁴⁸

The introduction of tiered financial reporting in the *ACNC Bill* aims to reduce compliance burdens and promote transparency through the ‘report-once, use often’ approach.⁹⁴⁹ Once the ACNC receives an entity’s financial account, the public will be able to assess its financial information through a central public information portal,⁹⁵⁰ which is line with recommendation 6.6 from the Product Commission’s report.

Non-compliance by an entity with any provisions relating to financial records and governance and external conduct standards may incur a civil penalty.⁹⁵¹ Before examining the enforcement powers of the ACNC, it is worth examining the introduction of governance and external conduct standards to increase the public’s confidence in the sector, about which much has been made.

8.3.6 Governance and External Conduct Standards

The *ACNC Act* seeks to create a minimum level of governance standards to increase the public’s confidence in the sector. This is to be achieved by an entity demonstrating how it pursues its purpose and manages its affairs in a manner that is open, accountable and transparent, all of which will minimise the risk of mismanagement and misappropriation.⁹⁵² Achieving these principle-based governance standards is to be specified in the regulations – but, at the time of

⁹⁴⁵ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-25.

⁹⁴⁶ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-25(1). Revenue is calculated with accordance with accounting standards in force at the relevant time. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-25(4).

⁹⁴⁷ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-25(2).

⁹⁴⁸ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 205-15(3).

⁹⁴⁹ Explanatory Material, *Australian Charities and Not-for-Profits Commission Bill 2012* Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.55, 233.

⁹⁵⁰ Australian Government Budget 2011-12, Budget Paper No.2 – Part 2: Expense Measures <http://www.budget.gov.au/2011-12/content/bp2/html/bp2_expens-22.htm> 4.

⁹⁵¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 90-5.

⁹⁵² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 45-1. The public includes donors, members and volunteers of an entity. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 45-5(1).

writing this thesis, the regulations to *ACNC Bill and ACNC Act* were not available.⁹⁵³ However, draft governance standards were released for public consultation.⁹⁵⁴ Similar to the financial reporting obligations, the governance standards are not applicable to all entities.⁹⁵⁵

The *ACNC Act* allows basic religious charities and small entities to be exempt from the prescribed governance standards.⁹⁵⁶ Furthermore, the Commissioner has the discretionary power to decide which specific governance standards will or will not apply to certain entities.⁹⁵⁷ The Commission's decision will be influenced by: what is reasonable for an entity to implement; an entity's circumstances; and the size and level of an entity's donations, grants and other monies received from the public or government.⁹⁵⁸ The rationale behind these varying expectations is based on the presumption that larger entities receive more public monies and are at greater risk of funds being mismanaged than smaller entities.⁹⁵⁹ The varying treatment of entities under the *ACNC Act* also applies to the external conduct standard provisions.

The external conduct standards outlined in the *ACNC Bill* will only apply to an entity that transfers funds and engages in activities outside Australia.⁹⁶⁰ These standards aim to prevent entities from supporting or contributing to terrorist or criminal activities.⁹⁶¹ The pending accompanying regulations will prescribe the external conduct standards; however, the regulations were not available at the time of writing this thesis. Similar to the governance standard provisions, the Commissioner will decide which standards will or will not apply giving regard to

⁹⁵³ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 5.29, 52.

⁹⁵⁴ The draft governance standards are outside the scope of this thesis. However, submissions have been made to Treasury and can be access at:
<http://www.treasury.gov.au/~media/Treasury/Consultations%20and%20Reviews/2012/Governance%20Standards%20for%20the%20Not-for-profit%20Sector/Submissions/PDF/065_Weinert_Kim_Danielle.ashx>

⁹⁵⁵ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 5.31, 5.36, 52–53.

⁹⁵⁶ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 45-15(3)-(5).

⁹⁵⁷ *ACNC Bill* ch 3 pt 3-1 dv 45 cl 45-10(4). Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 5.44-5.47, 53. See Table 10 for an explanation of what constitutes a large and small entity.

⁹⁵⁸ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 45-15(2A); Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 4.41–5.43, 53.

⁹⁵⁹ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 5.44–5.47, 53.

⁹⁶⁰ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 50-5(1)(a).

⁹⁶¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 50-5(1)(a)-(b).

an entity's size, and the extent it receives monies from the public or government.⁹⁶² Failure to comply with these governance standards, or to submit false financial records the Commissioner, may penalise an entity.

8.4 Enforcement Powers of the ACNC

The ACNC has the power to issue formal warnings if the Commissioner reasonably believes that an entity has, or is likely to, contravene the *ACNC Act*.⁹⁶³ Subsequent to issuing a warning, the Commission has the power to direct an entity to do a specified act, address the contravention and/or non-compliance of the *ACNC Act*, and not to enter into specified commercial transactions.⁹⁶⁴ In the event an entity fails to satisfy the Commissioner's directions, the Commissioner may issue an enforceable undertaking⁹⁶⁵ – for example, suspending or removing an entity from the registry.⁹⁶⁶ The Commissioner is obliged to use the ACNC's regulatory powers in a proportionate manner and, further, the Commissioner has the discretionary powers to impose administrative penalties.⁹⁶⁷

The Commissioner's discretionary powers include the ability to increase or decrease the amount of an administrative penalty based on the culpability and the actions of an entity.⁹⁶⁸ The *ACNC Act* provides the Commissioner with the option to increase a penalty by 20 per cent in the event an entity or its agent prepare a statement which is reckless, without reasonable care, or contains false, or misleading information.⁹⁶⁹ Conversely, the Commissioner may reduce a civil penalty by 20 per cent where an entity informs the ACNC of their false or misleading

⁹⁶² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 50-10(2A); Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 5.66–5.67, 55.

⁹⁶³ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 95-5.

⁹⁶⁴ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 100-60. The term 'specified act' is not defined in the *ACNC Bill* or the *ACNC Act*.

⁹⁶⁵ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) ss 90-1-90-15.

⁹⁶⁶ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 100-5.

⁹⁶⁷ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) ss 175-30 and 175-60; Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 13.95, 188.

⁹⁶⁸ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-30; Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 13.102, 189.

⁹⁶⁹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-25.

statement.⁹⁷⁰ The Commissioner's calculations of a base penalty amount are on a sliding scale, which are outlined in Table 10.

Table 10 – Base penalty amount⁹⁷¹

Item	Situation	Base Penalty Amount
1	The entity or its agent provides a statement that is false or misleading because of an intentional disregard of this <i>Act</i> .	60 Penalty Units ⁹⁷²
2	The entity or its agents provides a statement that is false or misleading because of recklessness as to the operation of the <i>Act</i> .	40 Penalty Units
3	An entity or its agent provides a misleading or false statement because of a failure to take reasonable care to comply with this <i>Act</i> .	20 Penalty Units

The *ACNC Act* also sets out penalties for an entity when it fails to lodge documents on time.⁹⁷³ Similar to the other administrative penalty provisions, the Commissioner has the power to impose a higher penalty for medium- and large-sized entities.⁹⁷⁴ Medium entities may face a penalty double the base penalty amount, and a large entity will be faced with a penalty of five times the base penalty amount.⁹⁷⁵ The maximum penalty, which the Commissioner may impose, can be no more than five penalty units, and an entity will have 14 days to pay any penalty.⁹⁷⁶ Should the penalty remains unpaid, a daily general rate of interest will incur,⁹⁷⁷ and it is treated as a tax-debt that the ATO will collect.⁹⁷⁸ Where the Commissioner has imposed a penalty, the Commissioner has the discretion to remit all or part of it.⁹⁷⁹ Administrative decisions made by the Commissioner may be subject to review and appeal where an entity feels dissatisfied.⁹⁸⁰

⁹⁷⁰ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-30.

⁹⁷¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-20.

⁹⁷² The current value of one penalty unit is \$110.00. *Crimes Act 1914* (Cth) s 4AA.

⁹⁷³ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) sub dv 175-C.

⁹⁷⁴ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-40(1).

⁹⁷⁵ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-40(1)(a)-(b), 45-15(2A). A base penalty amount is one penalty unit for a period of 28 days. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-40(2).

⁹⁷⁶ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-55.

⁹⁷⁷ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-65.

⁹⁷⁸ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-70.

⁹⁷⁹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 175-60.

⁹⁸⁰ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 160-5.

8.5 Reviewing the Commissioner's Decisions

An entity may lodge an objection within 60 days of receiving an administrative decision, and the entity must state in full the grounds on which the entity relies.⁹⁸¹ The Commissioner will decide whether or not to uphold an entity's request for a review.⁹⁸² This decision is referred to in the *ACNC Act* as an 'objection decision'.⁹⁸³ When the Commission has made the decision to review, it must then decide to allow the objection in full or in part.⁹⁸⁴ Should an entity disagree with the Commissioner's objection decision, it may apply to the Administrative Appeals Tribunal or to a designated court for a review or appeal the Commissioner's decision.⁹⁸⁵

8.6 Conclusion

Reforming Australia's not-for-profit sector at the federal level is something the sector has needed. Despite numerous federal government reports and inquiries detailing a number of key recommendations on how to best reform the sector (often repeating and/or echoing the same ones from the preceding report), reform has been slow and delivered piecemeal.

The centrepiece of the federal government's reform package is the creation of the ACNC. This body is tasked with regulating not-for-profit entities, and deciding which qualify for registration with the Commission. The ACNC's structure entails an advisory board and a Commissioner, and is tasked to enhance the public's trust and confidence in the sector through the regulatory framework of the ACNC. The Commissioner has two very general functions: to register and to monitor entities. The registration of certain types of entities is prescribed under the *ACNC Act* and, furthermore, an entity's registration is a prerequisite for it to access Commonwealth tax concessions and other government exemptions, benefits and concessions. Once an entity is registered, the Commissioner can carry out the ACNC's other general function to monitor entities.

⁹⁸¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 160-10(1).

⁹⁸² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 160-10(4).

⁹⁸³ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 160-15(2).

⁹⁸⁴ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 160-15(1).

⁹⁸⁵ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 160-25. 45-15(2A). The *ACNC Act* does not offer any guidance as to what is a designated court. However, the *ACNC Bill* stated that a court means the Federal Court of Australia or a Supreme Court that has jurisdiction in relation to matters arising under this *Act*. *ACNC Bill* ch 8 pt 8-2 dv 900 cl 900-5. However, the *ACNC Bill* does not contain any provisions that provide the state courts with the jurisdictional power to deal with reviewable or appealable matter under the *ACNC Bill*.

The monitoring of an entity is achieved through it submitting an annual report, which includes a financial report. However, small and basic religious entities appears to fall outside the monitoring powers of the ACNC, as they are exempt from submitting an annual financial report and are not subject to the governance and external conduct standards under the *ACNC Act*. Therefore, the Commissioner's monitoring function is confined to medium- and large-sized entities. Furthermore, the Commissioner is provided with discretionary powers to decide which governance and external conduct standards will be or will not be applicable to medium and large entities.

Additional discretionary powers for the Commission are evident where it exercises its enforcement powers. The Commissioner may increase or decrease the amount of a base penalty. The Commissioner has been provided with the statutory power to impose penalties upon entities where they fail to submit financial reports, or when a submitted financial report is prepared recklessly, without reasonable care, and/or contains false or misleading information. The ACNC has been established to achieve transparency and accountability within the sector to restore the public's confidence; however, there remain concerns about whether the ACNC will achieve transparency, and this is discussed in the next chapter.

CHAPTER 9: Conclusion

Evaluation of Australia's Recent Reforms Regarding Charities

*The future of the sector rests on its ability to engage the community in supporting its purpose.*⁹⁸⁶

9.0 Introduction

This chapter compares the functions and the power of the Australian Charities and Not-for-Profits Commission with the United Kingdom's Charities Commission, and reveals several limitations to Australia's proposed regulatory framework. These limitations are a direct consequence of the federal government implementing reform primarily to support its social inclusion policy – rather than reforming the sector to equip it for future challenges.

Australia's social inclusion policy appears to be modelled on the United Kingdom's *Big Society* policy. This chapter analyses the fiscal paradigm between not-for-profit organisations and government created by social inclusion policies. Lastly, this chapter discusses the known pitfalls that social inclusion policies has on the sector and assesses whether Australia is taking the appropriate strategic action to avoid these pitfalls.

9.1 Are These Reforms Measuring Up?

The federal government has pursued the reform of the not-for-profit sector, and the choices and decisions it has made are surprising. Although the *ACNC Act* remains a work in progress (hopefully), the reform picture remains incomplete. The federal government has articulated many goals to improve the administration of the sector by establishing the ACNC;⁹⁸⁷ however, there are some deficiencies with the *ACNC Act*.

The overall function of the ACNC is unclear, as the *ACNC Act* does not provide any specific details on the Commissioner's functions besides the general administration of the *Act*, registering

⁹⁸⁶ Productivity Commission, 'Contribution of the Not-for-profit Sector' (Research Report, Productivity Commission, January 2010) xxxiii.

⁹⁸⁷ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012, 5.

and monitoring entities.⁹⁸⁸ These explanations of the ACNC's functions are very general when compared to the Commission's five specific functions under the *Charities Acts* of the United Kingdom.⁹⁸⁹ These five functions are clearly expressed and are wider than just assisting not-for-profit organisations to comply with statutory administrative requirements. The Commission's wider functions comprise remedial and proactive action in connection to charity abuses, and ensuring fundraising activities are legitimate.⁹⁹⁰ The functions of the ACNC should be revisited to be more prescriptive and to target perverse conduct within the sector. These prescriptive functions would better manage and promote the policy of transparency and accountability. Furthermore, to strengthen the ACNC's function, the *ACNC Act* should connect the ACNC's functions to its objectives – and the ACNC should demonstrate its own level of transparency.

The ACNC demands the sector be transparent – therefore, it is only reasonable that the peak regulator is also open and transparent. The Commissioner is required to furnish the Minister with an annual report about the ACNC's performance, to be presented to the federal parliament at the end of each financial year.⁹⁹¹ However, the *Act* does not provide clarity as to whether the ACNC's performance relates to financial performance and/or particulars of the its functions, such as the number of entities registered and deregistered, or complaints received and investigated. This imbalance needs to be addressed by having the ACNC provide information on its website demonstrating how the ACNC and the Commissioner are achieving the objects of the *Act*, and how well they are performing their functions and managing their financial affairs by way of an annual report.⁹⁹²

The United Kingdom Commission's annual report publishes in great detail how it is discharging its functions, how its objectives and duties are being met, and how it is managing its financial affairs.⁹⁹³ The Commission, like the ACNC, is required to furnish parliament with a report – but the Commission, additionally, must disclose its annual report to the public (available through the Commission's website), hold a public annual meeting three days after disclosing its

⁹⁸⁸ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) pt 5-1.

⁹⁸⁹ See *Charities Act 2011* (UK) c25, s 15.

⁹⁹⁰ *Charities Act 2011* (UK) c 25, s 15(1).

⁹⁹¹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 130-5.

⁹⁹² *Charities Act 2011* (UK) cl 25, sch 2 para 11.

⁹⁹³ *Charities Act 2011* (UK) cl 24, sch 2 para 11(1).

annual report, and advise the Crown on matters relating to its functions and objectives.⁹⁹⁴ The *ACNC Act* does not require public disclosure of the ACNC's report; however, the requirement to submit its the annual report to federal parliament may be the means of public disclosure – but this is not ideal. While the general contention has been not to copy the United Kingdom,⁹⁹⁵ the ACNC should, however, take the lead by being open and transparent in reporting its functions, activities and financial affairs, like the United Kingdom Commission. Should the primary aim of the ACNC be to promote openness and transparency, additional information and clarity is needed regarding the ACNC's status.

The *ACNC Bill* and *Act* offer no information about the status of the ACNC. The importance of knowing its status is to affirm its independence, and to free it from the direction and/or control of any minister of the Crown, or any government department. Preserving the ACNC's independence is crucially important, not only to protect the sector's boundaries, but to prevent the federal government using it to command and control the sector. This may not be the intention of the federal government, however, the *ACNC Act* must be amended to clarify the status of the ACNC. Perhaps the *ACNC Act* could have a provision similar to section 13(4) of the *Charities Act 2011* (UK), which allows the Commission to carry out its functions and makes decisions free from any interference from parliament, government and/or a government department –the ACNC should be afforded the same protection.⁹⁹⁶

Further, the *ACNC Act* could simplify the meaning of a not-for-profit organisation by adopting the structural-operational definition, which is conceptually clearer than the definition contained in tax legislation. Directly adopting the structural-operational definition in the *ACNC Act* would remove the confusing and unnecessary reference to the two *Income Tax Assessment* Acts. The *ACNC Act*'s introduction of an 'entity' and a 'subtype of entity' has been purposely designed to support the government's National Compact framework⁹⁹⁷ and to overcome the High Court's decision of *Aid/Watch Incorporated v. Commission of Taxation*.⁹⁹⁸ Although there have

⁹⁹⁴ *Charities Act 2011* (UK) cl 25, s 15(1), sch 2 para 12. See also The Charity Commission Annual Report and Accounts 2011-12 (for the year ended 31 March 2012) at < http://www.charity-commission.gov.uk/Library/about_us/Annual_report_2012.pdf>.

⁹⁹⁶ *Charities Act 2011* (U) c 25.

⁹⁹⁷ Australian Government, 'A Definition of Charity' (Consultation Paper, Australian Government, October 2011) 1.

⁹⁹⁸ Aid/Watch is an organisation to research, monitor and campaign about foreign aid. Specifically, Aid/Watch would hold various public debates and release reports critiquing the effectiveness of foreign aid. The Commissioner of Taxation removed Aid/Watch's concessional tax endorsement and its charitable institution

been a previous attempts by the federal parliament to introduce a statutory definition of charity, these attempts have had limited success.⁹⁹⁹ Despite the Henry Tax Review calling for the introduction of a modern statutory definition of charity, the *ACNC Bill*'s meaning of 'an entity' is not modern, nor is there an advancement of the traditional charitable purposes.¹⁰⁰⁰

Moreover, the *ACNC Act* ignores the core legal tests of the public benefit test and the doctrine of *cy-près*. The *ACNC Act* does not state whether the ACNC will take into consideration long-standing case law when making its determination of an entity's registration and charitable status. The public benefit test cannot be excluded for the fundamental reason that a public benefit is the hallmark of a charity, and it distinguishes a charity's activities from those of government and private organisations.¹⁰⁰¹ Additionally, in borderline cases where a trust may fail to be recognised as charitable, the *cy-près* doctrine may save the trust – therefore, it should not exclude this doctrine. However, it is clear that further development to simplify the meaning of an entity is needed along with further clarity in the area of financial reporting under the *ACNC Act*.

The existing financial reporting frameworks for not-for-profit organisations are complex and uncoordinated.¹⁰⁰² Currently, there are four types of reporting requirements for not-for-profit

status. The Commissioner was of the view that Aid/Watch itself did not distribute aid and the organisation's purpose was political and, therefore, not charitable. The High Court held that generating public debate is a charitable purpose as it contributes to the public's welfare. In making its decision, the High Court rejected following *McGovern v Attorney-General* [1982] CH 321 on the basis that Australia has no general doctrine that excludes political objects from charitable purposes. *Aid/Watch Incorporated v Commission of Taxation* [2010] HCA 42, 47–49. The federal government expressed its disagreement in the High Court's finding, giving the government another reason to introduce a new definition of 'charity'. See Australian Government, 'A Definition of Charity' (Consultation Paper, October 2011) 1–2; Australian Government, Budget 2011–12, 'Budget Paper No 1 – Part 1 Revenue Measures' <http://www.budget.gov.au/2001/content/bp2/html/bp2_revenue-0.7.htm> 11.

⁹⁹⁹ Senator Xenophon, on 13 May 2010, introduced to the federal Senate the *Tax Laws Amendment (Public Benefit Test) Bill 2010*. The Senator's bill sought to introduce a public benefit test. It was proposed that the benefit is for the public or a significant section of the public balanced against any detriment or harm that a charitable institution may cause when carrying out its activities. The traditional public benefit test could be re-named to the public detriment test. The debate on this bill was adjourned and referred to the Senate Standing Economics Legislation Committee for inquiry and the Senate Standing Committee for the Scrutiny Bills. Senator Xenophon's *Bill* was found to be too narrow in addressing a broad range of issues in religious and charitable organisations. This bill appears to remain in limbo and will disappear once the government introduces its bill. Senate Economics Legislation Committee, Parliament of Australia, *Tax Laws Amendment (Public Benefit Test) Bill 2010*, (September 2010) 1; *Tax Laws Amendment (Public Benefit Test) Bill 2010* cl 50-51(1), (2), lines 8–10, 11–17, 3.

¹⁰⁰⁰ See Recommendation 42, Report to the Treasurer – Australia's Future Tax System; Australian Government Budget 2011–12, 'Budget Paper No 1 – Part 1 Revenue Measures' <http://budget.gov.au/2001/content/bp2/html/bp2_revenue-0.7.htm> 11. Public consultation is being undertaken at the time of writing this thesis. There have been announcements that, from 1 July 2013, a new statutory definition of charity for all Commonwealth laws will be introduced. Australian Government, Office for Not-for-Profit Sector, 'Introducing a Statutory Definition of 'Charity'' (2 November 2011) <<http://www.notforprofit.gov.au/nfp-reform/not-profit-sector-reform/introducing-statutory-definition-'charity'>>.

¹⁰⁰¹ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 106.

¹⁰⁰² Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.30, 228.

organisations. The manner in which an organisation is to meet its reporting obligations is determined by the organisation's structure, government contracts, fundraising requirements, and endorsement for concessional taxation treatment.¹⁰⁰³ To overcome and reform these complex arrangements, the ACNC has been called upon to explore ways to minimise financial reporting requirements through harmonisation – but the *ACNC Act* and *Bill* does very little to accomplish this objective.¹⁰⁰⁴

The federal government has acted upon recommendation 6.1 from the Productivity Commission and amended the *Corporations Act 2001* (Cth) to reduce the vigorous financial reporting and auditing obligations, specifically for smaller organisations. The *Corporations Amendment (Corporate Reporting Reform) Act*¹⁰⁰⁵ introduces a tiered reporting framework for companies limited by guarantee only. Table 11 outlines the new tiered and reporting obligations for companies limited by guarantee, which does not reconcile to the amounts outlined in Table 9.

Table 11 – An overview of obligations for companies limited by guarantee¹⁰⁰⁶

Tier	Criteria	Obligations
1	Small company limited by guarantee with an annual revenue less than \$250,000 and with no deductible gift receipt (DGR) status. ¹⁰⁰⁷	Exempt from preparing: a financial or directors' report; a financial report audited; or notifying members of the reports. ¹⁰⁰⁸
2	Company limited by guarantee with an annual revenue less than \$250,000 that has DGR status; and company limited by guarantee with an annual revenue of more than \$250,000, but less than \$1 million, regardless of DGR status.	Must prepare a financial report, but the report need not be audited unless the company is a Commonwealth company (or subsidiary) or Commonwealth authority. The financial report need not be audited, but must be reviewed. A director's report is required, but contains fewer details than that required of other companies. Any member that elects to receive the reports must be provided with them.

¹⁰⁰³ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.33, 228.

¹⁰⁰⁴ Australian Government Budget 2011-12, Budget Paper No.2 – Part 2: Expense Measures
<http://www.budget.gov.au/2011-12/content/bp2/html/bp2_expens-22.htm> 4.

¹⁰⁰⁵ 2010 (Cth).

¹⁰⁰⁶ *Corporations Amendment (Corporate Reporting Reform) Act 2010* (Cth) s 258A.

¹⁰⁰⁷ *Corporations Amendment (Corporate Reporting Reform) Act 2010* (Cth) s 54B.

¹⁰⁰⁸ Under section 294B, a small company limited by guarantee may be directed by ASIC to prepare financial and director's reports, audit the financial report, and to notify members of those reports. Failure to comply with ASIC direction is an offence based on strict liability. *Corporations Amendment (Corporate Reporting Reform) Act 2010* (Cth) s 294B(2).

3	Company limited by guarantee with annual revenue of \$1 million or more, regardless of the company's DGR status.	Must prepare financial and directors' reports (lesser details than what is required of other companies). ¹⁰⁰⁹ Financial report must be audited, and reports must be given to members who elect to receive them.
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Since these amendments have been in place, it has been reported that this tiered reporting system is onerous.¹⁰¹⁰ The system introduced by the *Corporation Amendment (Corporate Reporting Reform) Act 2010* (Cth) has added to the existing complex arrangements and further burdened not-for-profit organisations with higher compliance costs.¹⁰¹¹ These monetary thresholds are inconsistent with those for incorporated associations that operate in those jurisdictions with a tiered reporting framework; this highlights how harmonisation is not being achieved. Furthermore, the *ACNC Act* also affixes another framework of financial reporting for those entities under the ACNC's supervision, and it is difficult to ascertain which reporting framework applies.¹⁰¹²

The duplication of registration will have incorporated associations subject to the ACNC's supervision and also to the supervision of the respective state departments. Clearly, the desire to harmonise financial reporting obligations and reduce compliance costs for not-for-profit organisations will not be accomplished, since the *ACNC Act* only increases compliance costs and creates further administrative complexities for not-for-profit organisations.

Additional administrative requirements for an entity are the governance standards that the *ACNC Act* will impose. These are aimed at setting minimal standards to maintain, protect and enhance transparency and confidence in the not-for-profit sector. However, medium and large

¹⁰⁰⁹ Tier 3 organisations are required to provide an annual director's report, which is a simplified report containing: (i) a description of the entity's short- and long-term objectives; (ii) an outline of the entity's strategy for achieving these objectives; (iii) details of the entity's principal activities; (iv) how the principal activities assisted in achieving the entity's objectives; (v) how the entity measures its performance (including key performance indicators used by it); (vi) the name of each director at any time during or since the end of the year, and the period for which the person was a director; (vii) each director's qualification, experience and social responsibilities; (viii) the number of meetings of the board of directors held during the year, and each director's attendance at those meetings; (ix) each class of membership; and (x) the total amount that members of the company are liable to contribute if the company is wound up. *Corporation Amendment (Corporate Reporting Reform) Act 2010* (Cth) s 300B.

¹⁰¹⁰ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.37, 229.

¹⁰¹¹ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.38, 229.

¹⁰¹² Once the accompanying Regulations come into effect, there are certain reporting requirements and duties under the *Corporations Act 2001* (Cth) that will be 'turned off' for a company limited by guarantee. At the time of writing this thesis, the introduction of the *ACNC Act* permits for the duplication of registration. Dv 2 *Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Act 2012* (Cth).

entities will only be afforded this protection due to the presumption that larger organisations are prone to abuse. This presumption is erroneous, as charity abuse are not confined to a particular size or form of a not-for-profit organisation.

Mismanagement and opportunistic behaviour within not-for-profit organisations happens because of their amenable structures, which permits a small number of people to have the exclusive power to manage and control the organisation's affairs – and this can be hidden from the membership base regardless of its size.¹⁰¹³ Sadly, abuses within all forms and sizes of not-for-profit organisations does occur, and regardless of the gravity of the misappropriation, small not-for-profit organisations should also be afforded as much protection as necessary to prevent one-off and/or systematic abuses. In fact, these can have a greater impact on smaller organisations due to their limited resources. The federal government must reconsider this subjective application of governance standards to better protect not-for-profit organisations of all sizes and forms, and the sector.

The promotion of regulations to achieve transparency, governance and accountability under the *ACNC Act* is limited to registration and the submission of an annual statement – the federal government's reforms fail to understand and address the major issues that greatly affect the sector:¹⁰¹⁴ managing risks and related parties' transactions; avoiding charity abuses; preserving the sector's independence; and, moreover, protecting an entity's property. The *ACNC Act* in its present form fails to address these core issues. While public registration of entities and the submission of an annual report are important features of a good governance framework, there remain, however, other equally important features that have been excluded. The *ACNC Act* could be improved by requiring entities to have robust internal processes and systems in place to manage risk and protect an organisation's property – such as the timely disclosure of material interests. Furthermore, at the centre of the governance framework are an entity's officers, and

¹⁰¹³ Kim Weinert, 'Is there a perfect environment for a villain and villainess to survive?' in Rachel Franks and Susan E. Meindi (eds), *The Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 53.

¹⁰¹⁴ However, at the time of writing this thesis, a consultation paper was issued for the development of governance standards. This thesis does not analyse or discuss the draft governance standards outlined in the federal government's consultation paper.

attention should be on these officers' behaviour in governing the entity.¹⁰¹⁵ An officer undertaking a role must follow specific legal duties that are important mechanisms of organisational governance, but which are excluded from the *ACNC Act* and will be found in the accompanying regulations.¹⁰¹⁶

The appealing characteristic of a not-for-profit organisation is the nature of the activities it pursues. These pursuits allow not-for-profit organisations to enjoy a high level of trust; they can be perceived as wholesome, and the people connected with them are considered to be selfless.¹⁰¹⁷ However, these ideals are challenged when reports emerge about self-interested conduct within not-for-profit organisations, and it is no longer acceptable to rely on a traditional presumption that not-for-profits and their officers always behave in a purely altruistic manner.¹⁰¹⁸ Therefore, the *ACNC Act* and not its regulations should include legal duties that impose clear rules to govern and prescribe how an individual in position of control should behave. While the *ACNC Act* does impose a duty to notify the ACNC of a breach of the *Act*, this legal duty does not go far enough to promote good governance.¹⁰¹⁹ The *ACNC Act* should clearly outline the manner in which an officer must act to promote and satisfy the entity's altruistic mission – which should be done in good faith, with due diligence, skill, prudence, and for proper purpose. Although these duties generally apply to corporations and to a trustee of a charity, the *ACNC Act* should include these duties and additional obligations on officers (and members) not to engage in conduct that could harm the public's trust and confidence in the not-for-profit sector and its organisations.¹⁰²⁰

¹⁰¹⁵ Adrian Cadbury, *Corporate Governance and Chairmanship: A Personal View* (Oxford University Press, 2002), 34. The term 'officer' is used here in the absence of the *ACNC Bill* identifying or describing an individual who is appointed and has the responsibility of controlling and managing an entity, such as a trustee or director.

¹⁰¹⁶ Ian Ramsay, *Corporate Governance and the Duties of Company Directors*, Centre for Corporate Law and Securities Regulation, Faculty of Law (University of Melbourne 1997) 10.

¹⁰¹⁷ Kim Weinert, 'Is there a perfect environment for a villain and villainess to survive?' in Rachel Franks and Susan E. Meindi (eds), *The Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 50.

¹⁰¹⁸ Kim Weinert, 'Is there a perfect environment for a villain and villainess to survive?' in Rachel Franks and Susan E. Meindi (eds), *The Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 50.

¹⁰¹⁹ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 65-5(2). An entity must inform the Commissioner of a name change, address for service, a change of its governing rules, an entity has ceased. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 65-5(1).

¹⁰²⁰ Kim Weinert, 'Is there a perfect environment for a villain and villainess to survive?' in Rachel Franks and Susan E. Meindi (eds), *The Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 54.

However, having a clear set of legal duties and obligations would be rendered ineffective without an effective regulatory body.¹⁰²¹

The *ACNC Act* provides the ACNC with the light regulatory powers to remove an entity from the registry; however, the ACNC does not have the power to remove, suspend, or disqualify an individual from an entity for misconduct. Similar to the Commission in the United Kingdom, the ACNC must have the ability to take necessary remedial and/or proactive action against an individual within an entity engaging in misconduct or mismanagement.¹⁰²² While the *ACNC Act* states that the regulatory powers will be used proportionately, the ACNC does not have the ability to remedy particular situations; this will allow an entity to continue operating and, moreover, to protect an entity's property.

The *ACNC Act* overlooks the importance of an entity needing to protect its property. The Commission has the power to vest a charity's property in a trust with an official custodian, and to appoint an interim manager and a receiver to protect the charity's property and manage its affairs.¹⁰²³ The *ACNC Act* should be amended to provide the ACNC with a similar power to Commission, which allows it to undertake any action it thinks is necessary to protect a charity and avoid it having to cease operation.

Furthermore, where an entity may have older constitutional documents, which may prevent it undertaking certain transactions, the Commissioner should be given the power to remedy these deficiencies with the ACNC (like the Commission) appointing a receiver or a manager. The Commission does have the power to direct an entity not to enter into a specified commercial or financial transaction, which would affect the business of the entity. However, it is unclear from the *ACNC Act* when the ACNC would need to use this power and, furthermore, there is a concern that this may take away an entity's freedom to enter into arrangements. Additionally, the *ACNC Act* should include provisions that aim to protect the entity's property (including funds) and allow it the freedom to determine for itself whether to enter particular transactions. The *ACNC Act* should incorporate provisions that provide the necessary checks and balances for an entity to seek

¹⁰²¹ Kim Weinert, 'Is there a perfect environment for a villain and villainess to survive?' in Rachel Franks and Susan E. Meindi (eds), *The Real and the Reflected: Heroes and Villains in Existent and Imagined Worlds* (Inter-Disciplinary Press, 2012) 54.

¹⁰²² *Charities Act 2006* (UK) c 50, s1B.

¹⁰²³ Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 34.

advice from a financial expert – particularly regarding high-risk transactions.¹⁰²⁴ Should the Commissioner be provided with remedial powers, this would strengthen the ACNC's ability to maintain and promote an effective not-for-profit sector.

Another means for the ACNC to promote confidence in the sector is by it assisting entities to comply and understand the *Act* through guidance and education.¹⁰²⁵ Such advice would only be available to registered entities and limited to how they are to comply with the *Act*. The ACNC should consider widening this function to be similar to the Charity Commission, which provides advice to all individuals and forms of not-for-profit organisations on how to best manage and administer an entity. The Commission also provides advice to trustees and members on how to manage internal disputes and incidences of mismanagement. The *ACNC Act* should be modified to allow the ACNC to offer entities the necessary advice and education on how to appropriately deal with issues that might hinder their effective operation and administration, and how to best manage an entity.

As an initial step towards regulating the sector, the *ACNC Bill* and *Act* do not convey their aims simply or with clarity. The *ACNC Act* needs to be written in a manner that allows volunteers to easily comprehend their requirements under the *Act*. Despite the desire of the sector's stakeholders for a single legislative regulated framework for all forms and sizes of not-for-profit organisations, the ACNC, ultimately, is a national registry for those entities operating in the federal system. Under these new arrangements, an entity may find itself being governed by more than one regulatory regime. The federal government's based its abandonment of a single regulator for the not-for-profit sector because the Commonwealth lacked the necessary constitutional power to create a national regulator.¹⁰²⁶

9.2 A Federal Takeover of the Not-for-Profit Sector

There is an argument that the Commonwealth does have the necessary constitutional power to make laws to regulate all not-for-profit organisations using its power under section 51(xx) of the

¹⁰²⁴ The United Kingdom has introduced this requirement where the charity uses its land as security for a loan. Alison MacLennan, *Blackstone's Guide to the Charities Act 2006* (Oxford University Press, 2007) 41.

¹⁰²⁵ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 15-5(2)(iii).

¹⁰²⁶ Explanatory Material, Australian Charities and Not-for-Profits Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.61, 234.

Constitution.¹⁰²⁷ Section 51(xx) allows the Commonwealth to make laws about trading or financial corporations. *Prime facie*, a not-for-profit organisation would not be considered to be either a constitutional corporation or a trading corporation due to the non-distributive characteristic. However, the *ACNC Act* states that a constitutional corporation is recognised as a registered entity with the ACNC.¹⁰²⁸ Therefore, it begs the question, can any form of a not-for-profit organisation be considered a trading and/or financial corporation for the purpose of section 51(xx) of the *Constitution*?

Determining the characterisation of a not-for-profit organisation as a trading and/or financial corporation – and within the reach of the section 51(xx) power – turns on the wording of section 51 and, the legal tests from the High Court of Australia the High Court. The words ‘trading’ and ‘financial’ found in section 51(xx) cannot be interpreted in a narrow or strict manner, but in its current and popular sense.¹⁰²⁹ The popular and current interpretation of the word of ‘trade’ is broader than what was denoted in 1900, and it refers to the organisation’s activities, which includes buying and selling, negotiations, bargains, transport for reward, the purchase or sale of money, credit, news or information, tangibles or intangibles.¹⁰³⁰ This wide list of activities captures the type of activities undertaken by not-for-profit organisations. For example, the Salvation Army provides credit through a no-interest loan scheme, and sells a wide-range of goods through their ‘Salvo Stores’.¹⁰³¹ The degree that a section 51(xx) corporation engages in trading activities must be significant.¹⁰³² Whether an entity can be characterised as a trading and/or financial corporation is determined by the nature of the organisation’s activities, whether they are actual or intended.¹⁰³³

¹⁰²⁷ *Commonwealth of Australia Constitution Act 1900* (Imp).

¹⁰²⁸ The *ACNC Act* refers to a constitutional corporation as a federal regulated entity. *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) ss 205-15-205-20.

¹⁰²⁹ *R v Judges of the Federal Court of Australia; Ex parte Western Australia National Football League* (1979) 143 CLR 190.

¹⁰³⁰ *R v Judges of the Federal Court of Australia; Ex parte Western Australia National Football League* (1979) 143 CLR 190; Patrick Keyzer, *Principles of Australian Constitutional Law* (LexisNexis Butterworths, 3rd ed, 2010) 152.

¹⁰³¹ See The Salvation Army, *No Interest Loan Scheme* <<http://www.salvationarmy.org.au/contactus/victoria-divisions/pathways/no-interest-loan-scheme.html?s=0>>; The Salvation Army, *The Salvos Stores* (2011) <http://www.salvationarmy.org.au/salvosstores/shop.html>>. Trading activities undertaken by a not-for-profit organisation will be complementary to the organisation’s altruistic purpose.

¹⁰³² *Actors and Announcers Equity Association v Fontana Films Pty Ltd* (1892) 183 CLR 323, 182-18; *Re Dingjan; Ex parte Wagner* (1995) 183 CLR 323, 346 (Dawson J).

¹⁰³³ *New South Wales v Commonwealth* (1990) 169 CLR 482.

In the case of *St George County Council*, the High Court had to determine whether the Council could be considered as a trading section 51(xx) corporation.¹⁰³⁴ The High Court characterised the Council's activities as having a public purpose and, rather than a private enterprise, its purpose should not be considered as a trading corporation.¹⁰³⁵ Menzies J went further to express (*in dicta*) that universities, water and sewage utilities, churches, councils and public authorities could not be characterised as trading corporations.¹⁰³⁶ A similar view was Gibbs CJ, who said that under the actual activities test, the Council did not engage in activities for-profit and, therefore, it was not a section 51(xx) corporation, as it was not set up for the purpose of engaging in trading activities.¹⁰³⁷ Entities under the *ACNC Act* (apart from a constitutional corporation) and incorporated associations legislation would clearly not be considered as trading corporations pursuant to the actual activities test. However, the use of the actual activities test by the High Court has become dormant.

The High Court's current and preferred approach in determining a section 51(xx) trading corporation is the significant activities test, which is seen in the decision of *Adamson*.¹⁰³⁸ The *Adamson* case involved the Western Australian Football League (WA League), an incorporated association to promote the game of Australian Rules Football with not-for-profit objectives. The WA League earned a substantial income from a variety of activities, such as matches, broadcasting, fees, advertising, and membership subscriptions. The majority of the HCA held that the WA League and its clubs were trading corporations owing to their activities.¹⁰³⁹ Barwick CJ, Mason and Jacobs JJ found that the WA League and its clubs had substantial trading activities, which formed a 'sufficiently significant proportion of its overall activities'.¹⁰⁴⁰ Moreover, Murphy J stated that a 'trading corporation may also be a sporting, religious, or a governmental body. As long as the trading is not insubstantial [*sic*] and the fact that trading is incidental to

¹⁰³⁴ *R v Trade Practices Tribunal; Ex parte St George County Council* (1974) 130 CLR 533.

¹⁰³⁵ *R v Trade Practices Tribunal; Ex parte St George County Council* (1974) 130 CLR 533, 561, 547 (McTiernan J).

¹⁰³⁶ *R v Trade Practices Tribunal; Ex parte St George County Council* (1974) 130 CLR 533.

¹⁰³⁷ *R v Trade Practices Tribunal; Ex parte St George County Council* (1974) 130 CLR 533, 562.

¹⁰³⁸ *R v Judges of the Federal Court of Australia; Ex parte Western Australian National Football League* (1979) 143 CLR 190.

¹⁰³⁹ *R v Judges of the Federal Court of Australia; Ex parte Western Australian National Football League* (1979) 143 CLR 190, 233.

¹⁰⁴⁰ *R v Judges of the Federal Court of Australia; Ex parte Western Australian National Football League* (1979) 143 CLR 190, 208.

other activities it does not prevent it from being a trading corporation'.¹⁰⁴¹ Determining an organisation's activities as 'not insubstantial' has been subject to further discussions by the High Court.

The previous position of the courts was to determine an organisation's activities by finding an actual amount of monies earned by an organisation.¹⁰⁴² Wilcox J found that the Australian Red Cross earned \$2 million from the sale of goods and, therefore, it was a section 51(xx) trading corporation.¹⁰⁴³ However, in 2001, the idea of assessing an organisation's activity in dollars was rejected by the Full Federal Court in *Quickenden v O'Connor*.¹⁰⁴⁴

The *Quickenden* decision quantified an organisation's activities not in dollars, but in percentage.¹⁰⁴⁵ The trial court found that 28 per cent of the University of Western Australia's revenue was derived from trading activities.¹⁰⁴⁶ However, at trial, Carr J calculated the University's trading activities to be at 18 per cent, but either figure according to his Honour 'pointed to substantial trading activities'.¹⁰⁴⁷ Although the *Quickenden* decision does not provide a specific threshold figure as to what percentage of activities would constitute an insubstantial amount of trading activity, it would be possible, read in conjunction with *Adamson*, for a court to find 10 to 15 per cent of an organisation's revenue from its overall activities would be substantial enough for an organisation to be a s 51(xx) company.

Therefore, under the preferred significant activities test and, moreover, in light of Menzies' J and Gibbs' CJ reasoning, not-for-profit organisation are a trading corporation for the purpose of section 51(xx). This proposition is easily supported by the data from the ABS, which shows that during the 2006–2007 financial year, Australian not-for-profit organisations received \$6.1 billion of income; and the main source of income for not-for-profit organisations was from the sale of goods, which accounted for \$3.7 billion.¹⁰⁴⁸ There are many examples of not-for-profit

¹⁰⁴¹ *R v Judges of the Federal Court of Australia; Ex parte Western Australian National Football League* (1979) 143 CLR 190, 239.

¹⁰⁴² *E v Australian Red Cross Society* (1991) 27 FCR 310.

¹⁰⁴³ *E v Australian Red Cross Society* (1991) 27 FCR 310, 340-350.

¹⁰⁴⁴ (2001) 109 FCR 243.

¹⁰⁴⁵ *Quickenden v O'Connor* (2001) 109 FCR 243, 273.

¹⁰⁴⁶ *Quickenden v O'Connor* (2001) 109 FCR 243, 273.

¹⁰⁴⁷ *Quickenden v O'Connor* (2001) 109 FCR 243, 273.

¹⁰⁴⁸ Australian Bureau of Statistics, 810.6 – *Not-for-Profit Organisations, Australia 2006-07 – Other Activities* (12 June 2009) < [http://www.abs.gov.au/ausstats/abs@.nsf/Products/8106.0~2006-07+\(Re-Issue\)~Main+Features~Other+activities?OpenDocument](http://www.abs.gov.au/ausstats/abs@.nsf/Products/8106.0~2006-07+(Re-Issue)~Main+Features~Other+activities?OpenDocument)>.

organisations that heavily engage in trading activities incidental to their altruistic activities.¹⁰⁴⁹ Therefore, it is reasonably conceivable that the federal parliament can make laws with respect to not-for-profit organisations. Once a company has been recognised as a section 51(xx) corporation, the next question to ask is: what is the extent of the Commonwealth's regulation of trading corporations?

The Commonwealth has the power over trading and financial corporations that have already been formed.¹⁰⁵⁰ The *ACNC Act* does not confirm whether an entity becomes incorporated upon registering with the ACNC. While entities are incorporated either under the *Corporations Act 2001* (Cth) or the respective state association incorporated entities and engaging in significant trading activities, it is clear the Commonwealth has the constitutional power to regulate them. However, it remains unclear whether the Commonwealth can regulate the forms of the unincorporated association and charities. The Commonwealth does not have the power to incorporate charities and unincorporated associations under section 51(xx);¹⁰⁵¹ however, it is permissible for the Commonwealth to incorporate an organisation under section 51(i) where an organisation conducts interstate activity.¹⁰⁵²

Subsequent decisions of the High Court have disapproved and overturned this position, and it is now held that the federal government can regulate the activities of a trading section 51(xx) corporation, regardless of whether the trading corporation undertakes interstate trade.¹⁰⁵³ The High Court has expanded the scope of section 51(xx) by finding that the Commonwealth's corporation power is a plenary power and is to be constructed with all of its generality the words

¹⁰⁴⁹ There are an enormous number of not-for-profit organisations undertaking trading activities – too many to identify in this thesis. However, it has already been noted in this thesis the trading activities of the Salvation Army, which easily illustrates how these organisations could be considered section 51(xx) corporations. The federal government has undertaken steps to create a taxation policy regarding a not-for-profit organisation's unrelated commercial activities. This policy development has no impact on the argument regarding the legal test of 'not insignificant' activities in deeming an entity as a trading organisation under section 51(xx) of the *Constitution*. Commonwealth Government, *Better Targeting of Not-for-Profits Tax Concessions*, Consultation Paper, 27 May 2011.

¹⁰⁵⁰ *Parker & Co Pty Ltd v Moorehead* (1990) 8 CLR 330; *New South Wales v The Commonwealth* (1990) 169 CLR 482.

¹⁰⁵¹ *Strickland v Rocla Concrete Pipes Ltd* (1971) 124 CLR 468, 488 (Barwick CJ).

¹⁰⁵² *Australian Airways Pty Ltd v Commonwealth (No 1)* (1945) 71 CLR 29.

¹⁰⁵³ *Commonwealth v Tasmania* (1983) 158 CLR 1.

admit.¹⁰⁵⁴ Therefore, the High Court has held that the corporation power may be extended further to regulate *all* the activities and relationships of trading corporations.¹⁰⁵⁵

Furthermore, the High Court has found that section 51(xx) is not limited only to the federal parliament making laws regulating the activities to a trading corporation, but also to any matters that are significantly connected to a trading corporation.¹⁰⁵⁶ This finding by the High Court would permit the federal government to use section 51(xx) ‘as a peg upon which to hang legislation’ on matters that fall outside the Commonwealth’s strict subject matter.¹⁰⁵⁷ Therefore, the federal government has the power to regulate the activities of a not-for-profit’s members, its agents and donors.

There is no thus difficulty in identifying a not-for-profit organisation as a trading corporation in accordance to the significant activities test, and the Commonwealth has plenary power under section 51(xx) to regulate any activities of a not-for-profit organisations. Furthermore, the scope of this regulatory power is widened to catch any other matters that are significantly connected to a not-for-profit organisation and not confined to trading activities. This qualification shows that the federal government has the constitutional powers to achieve a single, national not-for-profit system, and a not-for-profit regulator.¹⁰⁵⁸ However, a federal takeover of the not-for-profit sector mirrors a WorkChoices situation, and a federal Labor government would be disinclined to exercise its constitutional power in this manner, which may be reminiscent of a WorkChoices’ electoral protest and defeat. The federal government’s reticence has it seeking out alternative ways to federally cover the not-for-profit sector.

¹⁰⁵⁴ *Commonwealth v Tasmania* (1983) 158 CLR 1 (McHugh and Gaudron J).

¹⁰⁵⁵ *Re Dingjan; Australian Workers’ Union v BHP Iron-Ore Pty Ltd* (2001) 106 FCR 482 (Gaudron, McHugh and Deane J).

¹⁰⁵⁶ *Re Dingjan* (1995) 183 CLR 323.

¹⁰⁵⁷ *Re Dingjan* (1995) 183 CLR 323 (Dawson J); *Murphyores Inc Pty Ltd v Commonwealth* (1976) 136 CLR 1.

¹⁰⁵⁸ The federal government could, by a federal takeover using their corporate power under the *Constitution*, streamline the registration process and reporting requirements for the sector by forming a specialised section within ASIC to regulate the activities of not-for-profit organisations. This would have omitted the government’s concern regarding the lack of constitutional powers to establish the ACNC. While it is clear that not-for-profit organisations are not, nor should be treated as for-profits, ASIC’s regulation of not-for-profits could have been designed to identify sector specific risks, respond to issues of non-compliance, and to intervene in matters to control or reduce these issues of risk and non-compliance. Moreover, this regulatory behavior must be carried out by ASIC in a manner appropriate to the sector’s uniqueness.

One way to establish a new federal regulatory system for the sector is through the referral powers of the states and territories.¹⁰⁵⁹ The states have already indicated their objection to a federal take over of incorporated associations. Therefore, the sensible alternative for the federal government in these circumstances is to encourage the states to harmonise their incorporation association legislation specifically in the areas of reporting arrangements and fundraising.¹⁰⁶⁰ However, as Appendix 1 illustrates, the states' reporting arrangements are not streamlined or harmonised and, in the jurisdictions of Tasmania and Western Australia, tiered reporting arrangement would need to be introduced. Harmonisation of state laws is soft reform, and the federal government reform plans ignore what the sector requires, which is wide, sweeping, revolutionary reforms.¹⁰⁶¹ Averse to a direct takeover of the sector, the federal government have structured the *ACNC Act* to facilitate an incremental takeover of the sector.

The objects' provisions of the *ACNC Act* facilitates an incremental takeover of the sector by the federal government. Pursuant to the *ACNC Act* not-for-profit organisations *must* register with the ACNC to receive Commonwealth tax concessions and other exemptions and benefits (my emphasis).¹⁰⁶² This prerequisite in the *ACNC Act* will result in every Australian not-for-profit organisation, of all forms and sizes, registering with the ACNC, despite the Explanatory Material to the *ACNC Bill* emphasising that registration with ACNC is voluntary.¹⁰⁶³ This requirement under the *ACNC Act* effectively conscripts not-for-profit organisations into the federal system and jurisdiction. The ACNC system of regulation, as already pointed out, adds another level of bureaucracy for organisations registered already in the existing system (being ASIC and the respecting states' executive departments). Complying with the new requirements of the ACNC, as well as the administrative requirements of the existing systems, will, over time, prove to be too difficult and burdensome for many not-for-profit organisations to navigate and meet the

¹⁰⁵⁹ Explanatory Material, Australian Charities and Not-for-Profit Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.62, 234.

¹⁰⁶⁰ Explanatory Material, Australian Charities and Not-for-Profit Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 17.63, 234-235.

¹⁰⁶¹ Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, Productivity Commission, January 2010), 147.

¹⁰⁶² *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 20-5.

¹⁰⁶³ Explanatory Material, Australian Charities and Not-for-Profit Commission Bill 2012 Australian Charities and Not-for-Profits Commission (Consequential and Transitional) Bill 2012 3.10, 25.

increasing administrative requirements.¹⁰⁶⁴ Consequently, not-for-profit organisations will abandon the state system for the reason that registering with the ACNC is linked to tax concessions and other government funding, such as government service delivery contracts, which many not-for-profit organisations need and heavily rely upon. Ultimately, the design of the ACNC is to serve the core purpose of implementing the federal government's social inclusions policy and agenda.¹⁰⁶⁵

9.3 Social Inclusion Policy

Social inclusion policies are not a new concept for western governments and, essentially, involve governments seeking to share the responsibility of providing social and welfare services with not-for-profit organisations.¹⁰⁶⁶ The structure behind a government's social inclusion agenda is the National Compact, which provides a framework to allow not-for-profit organisations, in collaboration with the federal government, to find innovative ways to deliver services and programs to the socially disadvantaged.¹⁰⁶⁷

The Compact's framework is designed to reflect a modern regulatory environment consisting of a registry and a regulatory body, which grants and revokes charitable exemptions.¹⁰⁶⁸ While these mechanisms can be seen in the ACNC framework, however, it remains to be seen whether this proposed environment could withstand the known problems of the social inclusion agenda.

9.4 Troubles with the Social Inclusion Agenda

The main consequence for not-for-profit organisations being enticed into a partnership with government is a phenomenon referred to as the 'contract culture'.¹⁰⁶⁹ This is the term used to describe a shift in how not-for-profit organisations secure funding. Traditionally, these

¹⁰⁶⁴ Furthermore, the *ACNC Act* needs to offer clearer incentives for entities to voluntarily register with the ACNC such as, limited liability.

¹⁰⁶⁵ Commonwealth Government, Office of the Not-for-Profit Sector, 'Not-for-Profit Sector Reform' <<http://www.notforprofit.gov.au/office-not-for-profit-sector>>.

¹⁰⁶⁶ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 155.

¹⁰⁶⁷ Commonwealth Government, 'National Compact: Working Together' (2010) 5–7.

¹⁰⁶⁸ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 150.

¹⁰⁶⁹ Kerry O'Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 155.

organisations secured funding from the private sector and through grants,¹⁰⁷⁰ but now statutory funding has taken over the traditional funding sources.¹⁰⁷¹ Statutory funding involves the government ‘contracting out’, for a fee, to a not-for-profit organisation to provide services¹⁰⁷² that were once directly provided by the government.¹⁰⁷³ This neo-liberal way reduces the government’s role in providing welfare and community services¹⁰⁷⁴ and, in turn, the not-for-profit sector becomes the substitute provider of welfare services.¹⁰⁷⁵ Consequently, not-for-profit organisations have become highly dependent on statutory funding, and governments also have become highly reliant on not-for-profit organisations to deliver welfare services.¹⁰⁷⁶ This new construct has brought with it numerous implications for the sector and many not-for-profit organisations.

Governments frequently use terms like ‘collaborative’¹⁰⁷⁷ and ‘joint venture’ to describe this new construct.¹⁰⁷⁸ However, in reality, this relationship is far from collaborative – especially for

¹⁰⁷⁰ David Chater, ‘Coming in from the Cold? The Impact of the Contract Culture on Voluntary Sector Homeless Agencies in England’ (Voluntary Sector Working Paper No 10, London School of Economics and Political Science, Centre for Civil Society, June 2008) 7.

¹⁰⁷¹ Jeremy Kendall, *The Voluntary Sector: Comparative Perspectives in the UK* (Routledge, 2003) 78; Australian not-for-profit organisations receive \$4, 253 million or 55 per cent of their total income from government. Australian Bureau of Statics, *Australian National Accounts: Non-Profit Institutions Satellite Account 2006-07* <<http://www.abs.gov.au/AusStats/ABS@.nsf/Latestproducts/5256.0Main%20Features22006>>; Productivity Commission, ‘Contribution of the Not-for-Profit Sector’ (Research Report, Productivity Commission, January 2010), 302-303.

¹⁰⁷² Services provided by not-for-profit organisations are diverse: aged care; rehabilitation services; palliative care; mental health services; child, youth and family support; community and emergency housing; alcohol and drug services; Indigenous health; offender and prisoner related support; offender and prisoner related support; victim support; services to the homeless; sexual assault and domestic violence services and legal assistance. Productivity Commission, ‘Contribution of the Not-for-Profit Sector’ (Research Report, Productivity Commission, January 2010), 299.

¹⁰⁷³ David Chater, ‘Coming in from the Cold? The Impact of the Contract Culture on Voluntary Sector Homeless Agencies in England’ (Working Paper Number 10, London School of Economics and Political Science, Centre for Civil Society, June 2008) 7.

¹⁰⁷⁴ David Chater, ‘Coming in from the Cold? The Impact of the Contract Culture on Voluntary Sector Homeless Agencies in England’ (Working Paper No 10, London School of Economics and Political Science, Centre for Civil Society, June 2008) 7.

¹⁰⁷⁵ M. Taylor, *The Best of Both Worlds: The Voluntary Sector and Local Government* (York: Joseph Rowntree Foundation, 1997) 136.

¹⁰⁷⁶ Debra Morris, ‘Paying the Piper: The Contract Culture as Dependency Culture for Charities’ in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 122–123. Governments will engage not-for-profit organisations to deliver services because it is known that they can provide flexibility, value for money and can best target client groups. Productivity Commission, ‘Contribution of the Not-for-Profit Sector’ (Research Report, Productivity Commission, January 2010), 305.

¹⁰⁷⁷ Australian Government, *National Compact: Working Together* (2011) 2–3.

¹⁰⁷⁸ Productivity Commission, ‘Contribution of the Not-for-Profit Sector’ (Research Report, Productivity Commission, January 2010), 229; The Right Honourable David Cameron, ‘Big Society Speech’ (Speech delivered at Liverpool, United Kingdom, 19 July 2010) <<http://www.number10.gov.uk/news/big-society-speech/>>.

not-for-profit organisations. The more accurate description of the relationship between government and the not-for-profit organisations under this new construct is strictly legal and fiscal. The government, the purchaser, has the absolute power over not-for-profit organisations, the supplier.¹⁰⁷⁹ Since not-for-profit organisations are highly reliant on government contracts, a ‘quasi-market’ emerges and the government dictates this market’s operation.¹⁰⁸⁰ Funding is distributed within this market by the purchaser’s contract, which has created not only a culture of contract, but also a competitive tendering culture amongst not-for-profit organisations.¹⁰⁸¹

Some not-for-profit organisations are fortunate to be in a non-competitive niche due to the uniqueness of their services,¹⁰⁸² however, this is not always so. Many not-for-profit organisations find themselves in direct competition with other not-for-profit organisations (who provide similar services) and with commercial businesses to secure the government contract.¹⁰⁸³ This competition leads not-for-profit organisations to being concerned with market share and focused on improving their strategic positioning within this market.¹⁰⁸⁴ For not-for-profit organisations to remain in this market and to have financial security, being viable in this environment becomes a priority.¹⁰⁸⁵ Fearing the loss of financial security, not-for-profit organisations will make fundamental shifts in their organisational structure and values to satisfy the purchaser’s demands.¹⁰⁸⁶

Service-delivery contracts permit the government to legitimately monitor and exercise a degree of control over a not-for-profit organisation’s activities. These binding agreements will link funds to variables, such as the quality of service delivered and certain financial reporting

¹⁰⁷⁹ Debra Morris, ‘Charities in the Contract Culture: Survival of the Largest?’ (2000) 20(3) *Legal Studies* 409, 410.

¹⁰⁸⁰ Davidson, B ‘For Profits Organisations in Managed Markets for Human Services’ in King, D and Meagher, G (eds) *Paid Care in Australia: Politics, Profits and Practice* (Sydney University Press, 2009) 43.

¹⁰⁸¹ Jonathon Gorten, *The Regulation of Organised Civil Society* (Hart, 2009) 98.

¹⁰⁸² Jonathan Roberts, ‘Partners or Instruments: Can the Compact guard the Independence and Autonomy of Voluntary Organisations?’ (Working Paper No 8, The London School of Economics and Political Science, Center for Civil Society, October 2007) 23.

¹⁰⁸³ Will Hutton and Stephen Bevan, ‘Pluralism in Public Service Delivery – The Role of the Third Sector’ in Association for Chief Executives of Voluntary Organisations, *Replacing the State. The Case for Third Sector Public Service Delivery* (ACEVO, 2003) 23.

¹⁰⁸⁴ Kerry O’Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 123.

¹⁰⁸⁵ Kerry O’Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 123.

¹⁰⁸⁶ Debra Morris, ‘Paying the Piper: The Contract Culture’ in Alison Dunn (ed) *The Voluntary Sector, the State and the Law* (Hart, 2000) 128.

mechanisms.¹⁰⁸⁷ While it may appear contractual conditions are forced upon a not-for-profit organisation, governments successfully argue that holding the provider to account ensures that public monies are being properly spent and allocated.¹⁰⁸⁸ However, with the government setting the agenda, and not-for-profit organisations heavily reliant on scarce government funding, many in the sector feel that governments intrude into their general management and goal-setting.¹⁰⁸⁹

Not only having to satisfy contractual obligations, a not-for-profit organisation also finds itself having to meet other demands from the government and, consequently, it changes its internal structure.¹⁰⁹⁰ Changes to an organisation's internal structure can be evidenced by the not-for-profit organisation becoming more central and bureaucratic,¹⁰⁹¹ which leads to it operating in a more formalised manner¹⁰⁹² and with an entrepreneurial edge.¹⁰⁹³ The implications from these internal shifts are two-fold:

1. A not-for-profit organisation responding to government demands, and not wanting to jeopardise this relationship, will undertake activities outside the organisation's original mission or trust instrument – this is referred to as 'mission drift'.¹⁰⁹⁴ Mission drift has both legal and taxation implications for a not-for-profit organisation –
 - a. The legal implication is that the organisation acts *ultra vires* and, therefore, contracts are void and unenforceable.¹⁰⁹⁵ In these circumstances, officers or trustees will be personally liable to the other contracting party for damages relating to a breach of warranty.¹⁰⁹⁶ Furthermore, an officer or trustee will be personally liable for a breach of

¹⁰⁸⁷ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 125.

¹⁰⁸⁸ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 125.

¹⁰⁸⁹ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 126–127.

¹⁰⁹⁰ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 128.

¹⁰⁹¹ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 133.

¹⁰⁹² Lynne Russell and Duncan Scott, 'The Impact of the Contract Culture on Volunteers' *Social Research* (Joseph Rowntree Foundation 1997) 1.

¹⁰⁹³ Associations of Chief Executive of Voluntary Organisations, '*Replacing the State? The Case for Third Sector Public Service Delivery*' (ACEVO, 2003) 5.

¹⁰⁹⁴ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 128.

¹⁰⁹⁵ Stephen Lloyd and Alice Walker, *Charities Trading and the Law* (Jordan, 2nd ed, 2009) 9.

¹⁰⁹⁶ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 130; *Re Boddeo* [1893] 1 Ch 547.

trust when acting outside the organisation's objectives.¹⁰⁹⁷ Contract culture not only has repercussions for the individual director or trustee, but also for the organisation itself.

- b. Where a not-for-profit organisation engages in unauthorised activities, it may risk losing its charitable or not-for-profit status.¹⁰⁹⁸ Should it engage in unauthorised activities in a limited capacity, then its status will not be affected.¹⁰⁹⁹ Where not-for-profit organisations carry on activities that are notably outside their mission, then it will lose its charitable status and will be taxed at a higher rate.¹¹⁰⁰ This 'take it or leave it' situation has brought about changes that also affect an organisation's members and volunteers.¹¹⁰¹

2. Under the government's contract, a not-for-profit organisation must deliver services efficiently, and many report that this requirement brings pressures that the organisation did not experience before the development of contracts.¹¹⁰² These pressures result in increased levels of responsibility and workload for volunteers and members.¹¹⁰³ To cope with this demand, the role of the volunteer has become more formalised, less autonomous, and subject to more supervision and performance reviews.¹¹⁰⁴ This has led to volunteers feeling demotivated, resulting in high turnover of volunteers and committee members.¹¹⁰⁵ Those remaining volunteers report that their role and participation becomes limited, and many are replaced by paid employees with the necessary skills and managerial experience¹¹⁰⁶ to achieve the performance outcomes stipulated in the government

¹⁰⁹⁷ Debra Morris, 'Charities and the Contract Culture: Partners or Contractors? Law and Practice in Conflict' (Charity Law Unit, University of Liverpool, July 1999) 2.

¹⁰⁹⁸ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 132.

¹⁰⁹⁹ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 131. This may be the position in the United Kingdom, however, it may not be so here in Australia as there are no Australian precedent to support how this issue would be decided.

¹¹⁰⁰ Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 131.

¹¹⁰¹ Debra Morris, 'Charities in the Contract Culture: Survival of the Largest?' (2000) 20(3) *Legal Studies* 409, 416.

¹¹⁰² Debra Morris, 'Paying the Piper: The Contract Culture as Dependency Culture for Charities' in Alison Dunn (ed), *The Voluntary Sector, the State and the Law* (Hart, 2000) 124.

¹¹⁰³ Lynne Russell and Duncan Scott, 'The Impact of the Contract Culture on Volunteers' *Social Research* (Joseph Rowntree Foundation, 1997) 1.

¹¹⁰⁴ Lynne Russell and Duncan Scott, 'The Impact of the Contract Culture on Volunteers' *Social Research* (Joseph Rowntree Foundation, 1997) 3.

¹¹⁰⁵ Lynne Russell and Duncan Scott, 'The Impact of the Contract Culture on Volunteers' *Social Research* (Joseph Rowntree Foundation, 1997) 3.

¹¹⁰⁶ Lynne Russell and Duncan Scott, 'The Impact of the Contract Culture on Volunteers' *Social Research* (Joseph Rowntree Foundation, 1997) 1.

contract.¹¹⁰⁷ This shift towards professionalism has contributed to the blurring between volunteers and paid employees,¹¹⁰⁸ causing tension between them.¹¹⁰⁹ Further, a not-for-profit organisation also finds itself having to provide more support to staff, especially volunteers. Organisations report that their resources have become strained by having to meet added costs for training and recruitment and other administrative needs.¹¹¹⁰ These tensions and strains have many reporting being ‘fatigued’ by government demands,¹¹¹¹ and this has led to tensions within the sector.¹¹¹²

Tension and anxiety at the sector level has led many not-for-profit organisations to feel constrained about challenging government policy.¹¹¹³ Many report they now have an inability to speak out and to advocate on behalf of their members about certain government policies, and this, in turn, impacts on the sector’s independence.¹¹¹⁴ The influence exerted on many not-for-profit organisations by government through contracts has also left organisations feeling obliged to take a contract on offer (even with no financial gain) for fear of being deselected.¹¹¹⁵ Guarding the sector’s independence is crucial to promoting a healthy democracy and having it operate as a counter balance to government and the private sector.¹¹¹⁶ The sector provides representation and a voice for particular individuals and/or communities to have their concerns properly taken into

¹¹⁰⁷ Debra Morris, ‘Paying the Piper: The Contract Culture as Dependency Culture for Charities’ in Alison Dunn (ed.), *The Voluntary Sector, the State and the Law* (Hart, 2000) 125.

¹¹⁰⁸ Lynne Russell and Duncan Scott, ‘The Impact of the Contract Culture on Volunteers’ *Social Research* (Joseph Rowntree Foundation 1997) 3.

¹¹⁰⁹ Debra Morris, ‘Charities in the Contract Culture: Survival of the Largest?’ (2000) 20(3) *Legal Studies* 409, 419.

¹¹¹⁰ Lynne Russell and Duncan Scott, ‘The Impact of the Contract Culture on Volunteers’ *Social Research* (Joseph Rowntree Foundation 1997) 3.

¹¹¹¹ Bristow, G., Entwistle, T., Hines, F. and Martin S., ‘Partnerships between the Public, Private and Voluntary Sectors in Wales’ (Research Report, Cardiff University: Centre for Local and Regional Government, 2003) in Graham Day, ‘The Independence of the Voluntary Sector in Wales’ (Working Paper No 3, The Baring Foundation, March 2009) 129 <<http://www.baringfoundation.org.uk/FirstPrincipleofVA.pdf>>.

¹¹¹² Julia Unwin, ‘Speaking Truth to Power – A Discussion Paper on the Third Sector’s Relationship with Government’ (ACEVO, 2004) 7.

¹¹¹³ Kerry O’Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 123.

¹¹¹⁴ Debra Morris, ‘Paying the Piper: The Contract Culture as Dependency Culture for Charities’ in Alison Dunn (ed.), *The Voluntary Sector, the State and the Law* (Hart, 2000) 126. See also the Charity Commission on the Future of the Voluntary Sector in England, ‘Meeting the Challenge of Change: Voluntary Action into the 21st Century’ (NCVO, 1996). Commonly referred to as the ‘Deakin Report’.

¹¹¹⁵ Julia Unwin, ‘Speaking Truth to Power – A Discussion Paper on the Third Sector’s Relationship with Government’ (ACEVO, 2004) 12-14.

¹¹¹⁶ Ann Blackmore, ‘Standing Apart, Working Together: A Study of the Myths and Realities of Voluntary and Community Sector Independence’ (NCVO, 2nd ed, 2008) 18.

account.¹¹¹⁷ This fundamental function is why ‘independence is the gold standard for the sector’.¹¹¹⁸

Despite not-for-profits having a legitimate interest in service delivery,¹¹¹⁹ it has caused the sector to fracture. The contract culture has split the sector into those organisations that deliver services under government contract, and those that do not. Organisations that do not deliver government services are considered to be on the ‘more ethereal side of civil society’.¹¹²⁰ This demarcation of the sector reinforces the perception that certain not-for-profit organisations are too close to government.¹¹²¹ Some with delivery services contracts report that their services reflect the political concerns of the purchaser, and the not-for-profit organisation finds itself occupying a space in the political arena and engaging in macro-level politics.¹¹²² This fracture is referred to as the ‘compact sector’.¹¹²³

The ‘compact sector’ brings another layer of risk to the sector’s diversity. Governments have a vested interest in ensuring that high standards are delivered by a not-for-profit organisation under the contract.¹¹²⁴ The manner in which these services are delivered has become indistinguishable from how the government provides services¹¹²⁵ – this has resulted in the sector becoming less diverse.¹¹²⁶

The cornerstone of the not-for-profit sector has always been its diversity and its independence, but the lines have now become blurred. The reshaping of the sector due to social inclusion policies is a confronting issue. Shifting from welfare to economics, the sector must

¹¹¹⁷ Ann Blackmore, ‘Standing Apart, Working Together: A Study of the Myths and Realities of Voluntary and Community Sector Independence’ (NCVO, 2nd ed, 2008) 18.

¹¹¹⁸ Nicholas Deakin, ‘Civil Society and Civil Renewal’ in Campbell Brown (ed) *Voluntary Action: Meeting the Challenges of the 21st Century* (NCVO, 2004) 30.

¹¹¹⁹ Ann Blackmore, ‘Standing Apart, Working Together: A Study of the Myths and Realities of Voluntary and Community Sector Independence’ (NCVO, 2nd ed, 2008) 18.

¹¹²⁰ Nicholas Deakin, ‘Civil Society and Civil Renewal’ in Campbell Brown (ed) *Voluntary Action: Meeting the Challenges of the 21st Century* (NCVO, 2004) 7.

¹¹²¹ Nicholas Deakin, ‘Civil Society and Civil Renewal’ in Campbell Brown (ed) *Voluntary Action: Meeting the Challenges of the 21st Century* (NCVO, 2004) 40.

¹¹²² Jonathon Gorton, *The Regulation of Organised Civil Society* (Hart, 2009) 61.

¹¹²³ Nicholas Deakin, ‘Civil Society and Civil Renewal’ in Campbell Brown (ed) *Voluntary Action: Meeting the Challenges of the 21st Century* (NCVO, 2004) 40.

¹¹²⁴ Nicholas Deakin, ‘Civil Society and Civil Renewal’ in Campbell Brown (ed) *Voluntary Action: Meeting the Challenges of the 21st Century* (NCVO, 2004) 29.

¹¹²⁵ Julia Unwin, ‘Beyond Service Delivery’ in *Replacing the State? The Case for Third Sector Public Service Delivery* (ACEVO, 2003) 13.

¹¹²⁶ Kerry O’Halloran, *Charity Law and Social Inclusion: An International Study* (Routledge, 2007) 123.

sustain its diversity and play a role in its reconfiguration by improving and balancing the partnership with government.¹¹²⁷ Good lessons can be learnt from the downfalls of social inclusion policy that occurred in the United Kingdom and, for Australia, these lessons are important to note as the not-for-profit sector enters into an uncharted paradigm with government,- it is crucial that the sector remains independent from government.

9.5 Is Australia going down the correct track?

For such a long time Australia's not-for-profit sector remained invisible to all levels of government. The federal government's reforms claim to enhance accountability and transparency within the sector; however, these matters are secondary, and these changes provide the seedbed for the government's social inclusion agenda and Compact document.

Generally, compacts are guides to good practice for the relationship between governments and not-for-profit organisations.¹¹²⁸ However, Australia's national Compact is not a guide to good practice, but an agreement between the federal government and the not-for-profit sector.¹¹²⁹ While signing-up to this agreement is non-compulsory, the federal government strongly encourages organisations to do so.¹¹³⁰ While this agreement is not a black-letter law contract – it would be very difficult to enforce this agreement owing to the language used – the compact does employ language that encourages not-for-profit organisations to sign it.

Platitudes are used throughout the Compact: 'working [sic] together'; 'partnership'; 'collaboration'; 'shared vision'; and other aspirational words. These outline generalities for the sector and the government to work together, such as to 'improve community wellbeing and a more inclusive Australian society.'¹¹³¹ Despite these motivating statements, the Compact fails to recognise the sector's independence.

¹¹²⁷ John Morison, 'The Government – Voluntary Sector Compacts: Governance, Governmentality and Civil Society' (2000) 27(1) *Journal of Law and Society* 99, 110–111.

¹¹²⁸ John Morison, 'The Government – Voluntary Sector Compacts: Governance, Governmentality and Civil Society' (2000) 27(1) *Journal of Law and Society* 99, 102.

¹¹²⁹ Australian Government, *National Compact: Working Together* (2010) 5.

¹¹³⁰ Australian Government, *National Compact*, 'How to Get Involved' <<http://www.nationalcompact.gov.au/how-get-involved>>.

¹¹³¹ Australian Government, *National Compact: Working Together* (2010) 5.

The Compact states that ‘signatories from the not-for-profit sector will [sic] agree to work with all Australian Government agencies to achieve these goals’.¹¹³² This language creates a top-down direction that may compromise the sector’s independence, as this takes away a not-for-profit organisation’s freedom to determine how to manage and deliver programmes for themselves, and not be influenced by departmental priorities. The Compact lacks the recognition that not-for-profit organisations operate in their own sphere, and many of these are in opposition to, rather than in partnership with, government.¹¹³³ While the Compact is very general, it is important that future re-drafted documents¹¹³⁴ move towards making specific undertakings to support the sector’s independence irrespective of the amount of funding given, or whether a not-for-profit organisation is a signatory to the Compact.¹¹³⁵

Further, the document makes reference to transparency and accountability within the sector being achieved through the Compact.¹¹³⁶ As a stand-alone document, it cannot achieve this; however, the ACNC has been created to make advances towards better transparency and accountability for the purpose of the Social Compact. Furthermore, the ACNC will also function as a point of contact between governments and registered entities undertaking government contracts and play a role in simplifying these interactions.¹¹³⁷ The true position of the ACNC seems to be elusive, and the *ACNC Act* sketches out a model that really serves the purpose of being a conduit between the government, and its agencies, and the not-for-profit organisations that are contracted to deliver government programs – this rather than the desired regulatory institution that would develop best practice standards for the sector. These changes in Australia centre on political opportunism rather than advancing the sector so it can be sustainable into the future. While the shifts in the sector are inevitable, further action and attention is needed to avoid

¹¹³² *National Compact, Working Together* (2010) 5.

¹¹³³ John Morison, ‘The Government – Voluntary Sector Compacts: Governance, Governmentality and Civil Society’ (2000) 27(1) *Journal of Law and Society* 99, 114.

¹¹³⁴ The compact notes that the document will need to be refined in the future. Commonwealth Government, *National Compact: Working Together*, 5.

¹¹³⁵ Compacts in the United Kingdom have moved away from general language and towards developing partnerships through specifics, such as resources and respecting confidentiality. John Morison, ‘The Government – Voluntary Sector Compacts: Governance, Governmentality and Civil Society’ (2000) 27(1) *Journal of Law and Society* 99, 115–116.

¹¹³⁶ Australian Government, *National Compact: Working Together* (2010) 9.

¹¹³⁷ *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) s 150–5(b).

it from being fractured and to prevent the emergence of contract, competition and compact cultures.¹¹³⁸

9.6 Conclusion

The ACNC, when compared to the United Kingdom's Commission, is complicated, and introduces an additional level of bureaucracy for not-for-profit organisations. This tangled arrangement could have been avoided had the federal government exercised its corporations powers under the *Constitution*. However, the shine of the ACNC is tarnished (albeit ever so slightly) when the federal government states that it has been established for the sole purpose of implementing and supporting the government's social inclusion policy – this despite the overwhelming call to restore public confidence in the sector through regulation.

The social inclusion policy entails not-for-profit organisations to deliver, for a fee, services that were once the responsibility by government, such as welfare, health and education. Through the national compact, not-for-profit organisations will agree to work and collaborate with the federal government to deliver services to marginalised groups within society. The language used in the national compact is non-specific, and warm words like 'partnership' and 'collaboration' are used throughout. The document is top-down driven, which raises concerns regarding the sector's independence.

Government using not-for-profit organisations as a vehicle for delivering services is not a new policy concept. The notable troubles of social inclusion policy are the contract, competition, compact cultures, which lead to the sector being fractured and its independence compromised. The federal government could prevent this fracturing by ensuring the sector's independence through the Compact and the *ACNC Act*, but until the federal government understands the importance of this, the opportunity to transform the sector for the future may be lost.

CONCLUDING REMARKS

¹¹³⁸ Section 73 of the *Charities Act 2006* (UK) allows a cabinet minister to appoint a person to undertake a review of the respective legislation. The *ACNC Bill* does not contain such a provision and, as this is a new concept for Australia, it would be important to have a similar provision which would allow a review of the ACNC and the *ACNC Act* as to its effectiveness and, furthermore, to consider any changes to improve its legal and regulatory framework.

The aim of this thesis was to examine the need for legal duties to be part of a governance framework to guide the conduct and behaviour of officers of a management committee within incorporated associations. Through an examination of legal duties within the respective state associations' legislation, this thesis discovered that not only are there inconsistencies across jurisdictions, but there are also serious gaps in the statutory framework. To identify some recognisable general legal duties and obligations, which could be imposed on an officer of a management committee, this thesis argued that an officer acts as an agent.

The respective associations statutes gives some support that an officer is an agent of the association with actual authority. Likewise the general law finds an officer of an unincorporated association may also be an agent. The finding that an officer of an unincorporated and incorporated association is a gratuitous agent means that there might be reluctance by a court to impose strict fiduciary obligations upon a volunteer. However, a gratuitous agent would be subject to a minimal standard of care expected of a competent agent in the circumstances. This thesis found that the standard of care is reflective of torts law and not fiduciary principle as such.

Inconsistency in the legal landscape for not-for-profit organisations is further shown in this thesis when the federal government reforms for the sector are examined. The main difficulty with the federal government's reform is its lack of coherence with the states and territories legislation. This thesis discusses how this problem could have been resolved if the federal government had exercised its plenary power under section 51(xx) of the *Commonwealth of Australia Constitution Act 1900* (Imp). Further, it was also expected that the federal government's reform would remedy the inconsistencies across jurisdictions and introduce a governance and regulatory framework based on the United Kingdom's model.

The United Kingdom modernised the sector to best assist not-for-profit organisations to efficiently achieve their mission in a demanding contemporary context. The Charity Commission was provided with additional power to function as a regulator, and advisor, an educator and an administrator – not only to charities, but also to the whole of the sector.

Acting as the sector's guardian the Commission emphasises that trustees and directors are not to breach their legal responsibilities and duties to the charity. The Commission in overseeing the not-for-profit sector must ensure that the management of a not-for-profit organisation is carried out in a manner that will not compromise confidence in the sector and its organisations. Ensuring proper management and transparency within a charity, this thesis examined the Commission's wide regulatory powers to remove, suspend and disqualify a trustee and/or member. When exercising its regulatory power, the Commission will do so proportionately and, moreover, they will work with a charity.

Reform undertaken by the federal government was not as extensive as the United Kingdom. This thesis analyses the reforms undertaken by the federal government to implement a regulatory framework for the sector. This analysis shows that Australia's regulatory framework is to serve the government's social inclusion policy – despite the overwhelming call to restore public confidence in the sector through regulation.

APPENDIX 1:

Tiered Financial Reporting Obligations for Incorporated Associations

Queensland

Description	Obligation
<p><i>Level 1</i> – An incorporated association that has:</p> <p>a) current assets of more than \$100,000; or b) total revenue of more than \$100,000.¹¹³⁹</p>	<p>Prepare a financial statement for its last reportable financial year that is audited by an auditor or an accountant.¹¹⁴⁰</p>
<p><i>Level 2</i> – An incorporated association that is not a level 1 incorporated association or a level 3 incorporated association.¹¹⁴¹</p>	<p>Prepare a financial statement audited by an auditor or an accountant. The financial statement and the signed audit report must be presented at the association's annual general meeting.¹¹⁴²</p>
<p><i>Level 3</i> – An incorporated association that has:</p> <p>a) current assets less than \$20000; and b) total revenue of less than \$20000.¹¹⁴³</p>	<p>Prepare a financial statement audited by an auditor or an accountant. The financial statement and the signed audit report must be presented at the association's annual general meeting.¹¹⁴⁴</p>

¹¹³⁹ *Total Revenue* – means the association's total income during the last financial year from all its activities before expenses, including the cost to the association of goods sold by it, are deducted. *Reportable Financial Year* – means the period starting on the day of incorporation and ending on the second end date after incorporation. *Associations Incorporation Act 1981 (Qld)* ss 58, 58A.

¹¹⁴⁰ *Associations Incorporation Act 1981 (Qld)* s 59.

¹¹⁴¹ *Associations Incorporation Act 1981 (Qld)* s 58.

¹¹⁴² *Associations Incorporation Act 1981 (Qld)* s 59.

¹¹⁴³ *Associations Incorporation Act 1981 (Qld)* s 58.

¹¹⁴⁴ *Associations Incorporation Act 1981 (Qld)* s 59.

New South Wales

Description	Obligation
<p><i>Tier 1</i> – Means any association whose:</p> <ul style="list-style-type: none"> a) gross receipts of the prescribed amount of \$250,000, or b) current assets of the prescribed amount of \$500,000.¹¹⁴⁵ 	<p>Financial statements must include:</p> <ul style="list-style-type: none"> a) details of any mortgages, charges and other securities affecting any property owned by the association; and b) a separate income and expenditure statement and balance sheet for each trust for which the association is the trustee.¹¹⁴⁶
<p><i>Tier 2</i> – any association that is not a Tier 1 association.¹¹⁴⁷</p>	<p>Financial statements to be prepared must include:</p> <ul style="list-style-type: none"> a) an income and expenditure statement and a balance sheet, which outlines the appropriately classified individual sources of income and individual expenses incurred in the operation of the association and the association's assets and liabilities; b) details of the association's mortgages, charges and other securities affecting any property owned by the association; c) a separate income and expenditure statement and balance sheet for each trust for which the association is the trustee.¹¹⁴⁸ <p>Financial statements must be submitted to the association's annual general meeting.¹¹⁴⁹</p>

¹¹⁴⁵ *Associations Incorporation Act 2009* (NSW) s 42(1); *Associations Incorporation Regulation 2010* (NSW) reg 7. Gross receipts for a financial year are equal to the total revenue recorded in the association's income and expenditure statement for that financial year. Assets (other than real property or assets capable of depreciation), which are held by the association, also including amounts, held in financial institutions, stocks and debentures. *Associations Incorporation Regulation 2010* (NSW) reg 7(1)-(2).

¹¹⁴⁶ *Associations Incorporation Regulation 2012* (NSW) reg 8(1).

¹¹⁴⁷ *Associations Incorporation Act 2009* (NSW) s 46.

¹¹⁴⁸ *Associations Incorporation Regulation 2010* (NSW) reg 9.

¹¹⁴⁹ *Associations Incorporation Act 2009* (NSW) s 48.

Description	Obligation
<p><i>Prescribed Association</i> – Means an association that has:</p> <p>a) gross receipts in that association's previous financial year more than \$200,000; or</p> <p>b) gross assets more than \$500,000.¹¹⁵¹</p>	<p>At the end of each financial year a prescribed association must have:</p> <p>a) its accounts audited by a registered company auditor, a firm of registered company auditors, a member of CPA Australia or the Institute of Chartered Accountants in Australia;</p> <p>b) the person who audits the accounts must provide the association with a written report of the audit.¹¹⁵²</p>

Description	Obligation
<p><i>Tier 1</i> – An association with revenue less than \$250,000</p>	<p>Tier 1 associations must prepare financial statements that are a true and fair view of the association's financial position and performance during and at the end of its last financial year.¹¹⁵³</p>

¹¹⁵⁰ Victorian incorporated associations must prepare financial statements in line with the *Associations Incorporation Reform Act 2012* (Vic), but only if the association's financial year commences after 30 June 2013. Consumer Affairs Victoria, 'Adapting to the New Incorporated Associations Laws' 25 June 2013 < <http://www.consumer.vic.gov.au/clubs-and-not-for-profits/incorporated-associations/adapting-to-the-new-laws#financial-statements>>.

¹¹⁵¹ *Associations Incorporation Act 1981* (Vic) s 3.

¹¹⁵² *Associations Incorporation Act 1981* (Vic) s 30B.

¹¹⁵³ *Associations Incorporation Reform Act 2012* (Vic) s 92. The financial statement that gives a true and fair view of the associations position is a prescribed form under the *Associations Incorporation Reform Regulations 2012* (Vic) reg 15, Sch 1.

<i>Tier 2</i> – An association with revenue between \$250,000 - \$1, 000,000	Tier 2 associations must prepare financial statements in accordance with the Australian Accounting Standards. ¹¹⁵⁴
<i>Tier 3</i> – An association with revenue of more than \$1,000,00	Tier 3 associations must a financial statements (in accordance with the Australian Accounting Standards) and an audit of financial statements (prepared by an independent person and in accordance with the Australian Auditing Standards). ¹¹⁵⁵

Northern Territory

Description	Obligation
<i>Tier 1</i> – An association that is not a Tier 1 or Tier 2 association.	Tier 1 incorporated associations must audit the association’s financial statements in accordance with applicable Australian Auditing Standards. ¹¹⁵⁶
<i>Tier 2</i> – An association that has: a) a prescribed amount of \$25,000 (gross receipts); and b) a prescribed amount of \$50,000 (gross assets). ¹¹⁵⁷	Tier 2 incorporated associations must audit the association’s financial statements in accordance with applicable Australian Auditing Standards. ¹¹⁵⁸
<i>Tier 3</i> – An association that has: a) a prescribed amount of \$25,000 (gross receipts); and b) a prescribed amount of \$50,000 (gross assets). ¹¹⁵⁹	Tier 3 incorporated associations must audit the association’s financial statements in accordance with applicable Australian Auditing Standards. ¹¹⁶⁰

¹¹⁵⁴ *Associations Incorporation Reform Act 2012* (Vic) s 95.

¹¹⁵⁵ *Associations Incorporation Reform Act 2012* (Vic) ss 98-99.

¹¹⁵⁶ *Associations Act 2003* (NT) s 46.

¹¹⁵⁷ *Associations Act 2003* (NT) s 47 (1)(a); *Associations Regulation 2004* (NT) reg 12.

¹¹⁵⁸ *Associations Act 2003* (NT) s 47; *Associations Regulations 2004* (NT) reg 11.

¹¹⁵⁹ *Associations Act 2003* (NT) s 48 (1)(c); *Associations Regulation 2004* (NT) reg 13.

¹¹⁶⁰ *Associations Act 2003* (NT) s 48; *Associations Regulations 2004* (NT) reg 11.

South Australia

Description	Obligation
<p><i>Prescribed Association</i> – is an incorporated association that had:</p> <p>a) gross receipts in the previous financial year in excess of \$500,000.¹¹⁶¹</p>	<p>A prescribed association must keep its accounting records in a manner that enables an association:</p> <p>a) present fair results of the operations of the association; and</p> <p>b) the accounts of the association to be conveniently and properly audited.¹¹⁶²</p>

¹¹⁶¹ *Associations Incorporation Act 1985* (SA) s 3(1) (a)(ii); *Incorporated Associations Regulations 2008* (SA) reg 4.

¹¹⁶² *Associations Incorporation Act 1985* (SA) s 35.

APPENDIX 2:

An Overview of Reason/s for Disqualification from Office

Jurisdiction	Qld	NSW	ACT	Vic	SA	WA	Tas	NT
Indictable Offences ¹¹⁶³	X	X	✓	X	✓	X	X	X
Fraud ¹¹⁶⁴	X	X	✓	X	✓	X	X	X
Unsound Mind ¹¹⁶⁵	X	✓	X	✓	X	X	X	X
Bankruptcy ¹¹⁶⁶	✓	✓	✓	✓	✓	X	✓	X
Death ¹¹⁶⁷	X	X	X	✓	X	X	✓	X
No Longer a Resident ¹¹⁶⁸	X	✓	X	✓	X	X	X	X
Imprisonment ¹¹⁶⁹	✓	X	X	X	X	X	X	X
Non-Compliance with the Act ¹¹⁷⁰	X	✓	✓	X	X	X	X	X

¹¹⁶³ Indictable offences relating to the promotion, formation or management of a body corporate. *Associations Incorporation Act 1991* (ACT) s 63(1)(a); *Associations Incorporation Act 1985* (SA) s 30(2)(c).

¹¹⁶⁴ Offences relating to fraud or dishonesty punishable by imprisonment of three months or more. *Associations Incorporation Act 1991* (ACT) s 63(i)(b); *Associations Incorporation Act 1985* (SA) s 30(2)(b).

¹¹⁶⁵ *Associations Incorporation Act 2009* (NSW) s 35(1)(e); *Associations Incorporation Act 1981* (Vic) s 27(e); *Associations Incorporation Reform Act 2012* (Vic) s 78(2)(c)(iii).

¹¹⁶⁶ *Associations Incorporation Act 1991* (ACT) s 63(2); *Associations Incorporation Act 1981* (Vic) s 27(d); *Associations Incorporation Reform Act 2012* (Vic) s 78(2)(c)(ii); *Associations Incorporation Act 2009* (NSW) s 35(1)(d); *Associations Incorporation Act 1985* (SA) s 30(1); *Associations Incorporation Act 1981* (Qld) s 61A(1A); *Associations Incorporation Act 1964* (Tas) s 14(5)(b) public officer only.

¹¹⁶⁷ *Associations Incorporation Act 1981* (Vic) s 27(2)(d); *Associations Incorporation Reform Act 2012* (Vic) s 78(2)(c)(i); *Associations Incorporation Act 2009* (NSW) s 35(1)(f); *Associations Incorporation Act 1964* (Tas) s 14(5)(e) public officer only.

¹¹⁶⁸ *Associations Incorporation Act 1981* (Vic) s 27(2)(d); *Associations Incorporation Reform Act 2012* (Vic) s 78(2)(c)(d), however this sub-provision now only applies to the association's secretary no longer residing in Australia; *Associations Incorporation Act 2009* (NSW) s 35(1)(f); *Associations Incorporation Act 1964* (Tas) s 14(5)(e) public officer only.

¹¹⁶⁹ On indictment and imprisoned summarily. *Associations Incorporation Act 1981* (Qld) s 61A(1)(a)(i)-(ii).

¹¹⁷⁰ *Associations Incorporation Act 1991* (ACT) s 63A; *Associations Incorporation Act 1985* (SA) s 30(2)(d)(i)-(iii).

APPENDIX 3:

The Principles of Public Benefit (United Kingdom)¹¹⁷¹

Principle 1 - There must be an identifiable benefit or benefits.

Principle 1a: *It must be clear what the benefits are.*

The benefit to the public should be capable of proof through factual and positive evidence where necessary. The benefit to the public is capable of being recognised, identified, defined, or described. Benefits that are easily quantified and measured are also considered.

Principle 1b: *The benefits are related to the aims.*

Assessing whether an organisation meets the public benefit requirement, the benefits considered are those that arises as a result of the organisation pursuing its charitable and stated aims (that falls within a listed charitable purpose). When an organisation is pursuing more than one aim, each one of those aims must meet the public benefit requirement.¹¹⁷²

Principle 1c: *Benefits must be balanced against any detriment or harm.*

This is an exercise of balancing the benefits against the detriment or harm. Should an organisation's activities have harmful consequences that are greater than the benefits, the organisation is not charitable. A charitable aim that is illegal, intentionally deceitful, or misrepresentative is a sham, and it cannot be charitable. Where there is detriment or harm present, the balancing exercise is not needed.

Principle 2 – Benefit must be to the public, or a section of the public

Principle 2a: *The beneficiaries must be appropriate to the aims.*

The term 'the public or section of the public' refers to a negligible number of people who can potentially benefit now and in the future. The class of people who can benefit must be a public class. The public class must be sufficiently large given the charitable aim is carried out and consideration is given to the organisation's available resources.

Principle 2b: *Where benefit is to a section of the public, the opportunity to benefit must not be unreasonably restricted.*

For restrictions to be reasonable they must be legitimate, proportionate, rational and justifiable to the nature of the organisation's charitable aims. Restrictions are evident from the way the organisation's objects are worded. Beyond the wording of the organisation's objects there are some reasonable restrictions that exist, such as:

Geographical restrictions – beneficiaries are defined by where they live;

Restrictions based on charitable need – beneficiaries can be defined by some common need (poverty, age, disability, etc.);

Restrictions based on personal characteristics – beneficiaries can be defined by reference to gender, race, religion, or other defining characteristic;

Restrictions based on access to facilities – limitations are placed on who can access facilities, what can accessed or degree of access that can be provided by a charity;

Restrictions based on eligibility to membership – members of a charity are beneficiaries under the charity's membership structure. Restrictions placed on who can join must be reasonable, justifiable and

¹¹⁷¹ Charity Commission, 'Charities and Public Benefit – The Charity Commission's General Guidance on Public Benefit' <<http://www.charity-commission.gov.uk/Library/guidance/publicbenefittext.pdf>>; Charity Commission, 'Analysis of the Law Underpinning Charities and Public Benefit' (December 2008) <<http://www.charity-commission.gov.uk/library/guidance/lawpb1208.pdf>>.

¹¹⁷² *Charities Act 2006* (UK) c 50, s 2, 3(2); *Charities Act 2011* (UK) c 25, s 4(2).

linked to the charity's aims.

Restrictions based on trustees' discretion – benefits are restricted to a particular group of people on the basis of trustees' exercising their discretion; and

Restrictions based on ability to pay any fees charged – the charging of fees has, in practice, restricts those who can afford to pay fees.

Should a restriction be considered reasonable, then it is accepted that society as a whole benefits in helping that section of society.

Principle 2c: *People in poverty must not be excluded from the opportunity to benefit.*

The term 'poverty' means people who are financially disadvantaged. Additionally, the term 'people in poverty' considers the context of an organisation's aims and if those aims are intended to benefit and where the organisation carries out its aims.

Principle 2d: *Any private benefits must be incidental.*

The term 'private benefits' refers to benefits received by people or organisations other than a beneficiary. A private benefit will be incidental if evidenced that an individual directly contributed towards achieving the charity's aims and/or it is a necessary result, or by-product of carrying out those items. This occurs only if the action was taken with the intention of furthering the charity's aims and, moreover, the private benefit is reasonable in the circumstances.

APPENDIX 4:

Recommendations and Government Response to the Report into Disclosure Regimes for Charities and Not-for-Profit Organisations¹¹⁷³

Recommendation 1

The committee recommends that all Australian Governments agree on common terminology for referring to organisations within the Sector. Governments should also develop a common meaning for terms referring to the size of these organisations, including ‘micro’, ‘small’, ‘medium’ and ‘large’. All government departments should adopt this standard terminology.

Commonwealth Government Response:

Agree in principle. The Commonwealth Government recognises the broad range of organisations that make up the third sector and the lack of clear terminology, particularly when various tax concessions are available. Common definitions and terminology will help to build a consistent view of the third sector and its operation within Australia. The results of the Productivity Commission’s Review of the contribution of the not-for-profit sector may assist in developing a framework, which could underpin standard definitions and terminology.

The Review of Australia’s future tax system (the ‘Henry Review’) may also examine the complex tax arrangements available to various types of organisations under the umbrella of the third sector and consider appropriate and alternative arrangements.

Recommendation 2

The committee recommends that the Government establish a unit within the Department of Prime Minister and Cabinet specifically to manage issues arising for Not-for-Profit Organisations. The unit should report to a Minister for the Third Sector.

Commonwealth Government Response:

Noted. The Social Inclusion Unit within the Department of the Prime Minister and Cabinet currently provides co-ordination on these issues across government. This recognises that other departments have responsibility that intersect with the third sector and are often more suited to provide overall policy guidance.

The Social Inclusion Unit reports to the Prime Minister and the Minister for Social Inclusion.

Recommendation 3

The committee recommends that there be a single independent national regulator for not-for-profit organisations.

¹¹⁷³ Senate Standing Committee on Economics, Parliament of Australia, *Disclosure Regimes for Charities and Not-for-Profit Organisations* (4 December 2008)
<http://www.aph.gov.au/Senate/Committee/economics.ctte/Charities_08/gov_response.pdf>.

Recommendation 4

The committee recommends that the Australian National Regulator for not-for-profit organisations should have similar functions to regulators overseas and particularly in the UK, including a Register for Not-for-Profit Organisations with a compulsory sign-up requirement. The committee recommends consultation with the Sector to formulate the duties of the National Regulator.

As a minimum, the Regulator should:

- a. Develop and maintain a Register of all not-for-profit organisations in Australia. Once registered, the Commission should issue each organisation with a unique identifying number or allow organisations with an ABN to use that number as their Not-for-Profit identifier. This would be enabled using existing ASIC website resources.
- b. Develop and maintain an accessible, searchable public interface.
- c. Undertake either an annual descriptive analysis of the organisations that it regulates or provide the required information annually to the ABS for collation and analysis.
- d. Secure compliance with the relevant legislation.
- e. Develop best practice standards for the operation of not-for-profit organisations.
- f. Educate/Advise not-for-profit organisations on best practice standards.
- g. Investigate complaints relating to the operations of the organisations.
- h. Educate the public about the role of the not-for-profit organisations.

The Regulator when implementing its own code of conduct should consider the voluntary codes of conduct developed by ACFID and FIA respectively.

Commonwealth Government Response to Recommendations 3 and 4:

Noted. The establishment of a single, independent national regulator, enacted by Commonwealth legislation, requires agreement by State and Territory Governments to refer to their responsibilities to the Commonwealth. It will be considered by Government, drawing on findings of reviews progressing throughout 2009 such as the Productivity Commission Review of the contribution of the not-for-profit sector.

Recommendation 5

The committee recommends that the Commonwealth Government develop the legislation that will be required in order to establish a national regulator for Australia.

Commonwealth Government Response to Recommendations 4 and 5:

Noted. The Council of Australian Government's Business Regulation and Competition Working Group ('COAG BRCWG') has included regulatory reform of the third sector as part of its 2009 work plan.

Recommending a national regulator, the Senate Committee has indicated that the office of the Registrar of Indigenous Corporations ('ORIC') which regulates Indigenous corporations under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* is a special measure for the advancement and protection of Aboriginal and Torres

Strait Islander people. Any consideration of ceasing ORIC or repealing the CATSI Act requires consideration of the impact this may have on Indigenous corporations and their unique role and function.

Recommendation 6

The committee recommends that, once a Register is established and populated, this information should be provided to the ABS, who should prepare and publish a comprehensive study to provide government with a clearer picture of the size and composition of the third sector.

Commonwealth Government Response:

Noted. The Productivity Commission Review of the contribution of the not-for-profit sector will consider, among other issues, alternatives for, or improvements in, measurements or further quantitative and or qualitative means of capturing the not-for-profit sector's full contribution to society.

The Australian Bureau of Statistics will be conducting a Non-Profit Institutions Satellite Account in 2009. This will provide important evidence relating to the contribution of the non-profit sector and feed into the Productivity Commission Review.

The outcome of this Productivity Commission Review will inform any decision regarding the establishment of, and use for, such a register.

Recommendation 7

The committee recommends that a single, mandatory, specialist legal structure be adopted for not-for-profit organisations through a referral of state and territory powers. Given the degree of change such as legal structure would mean for some not-for-profit organisations, the legal structure must be developed in full consultation with these organisations.

Commonwealth Government Response:

Noted. As with Recommendations 3, 4 and 5, the move to a single specialist legal structure requires agreement by State and Territory Governments to refer their responsibilities to the Commonwealth Government. It is an issue to be considered in light of reviews relating to the third sector taking place throughout 2009, such as the Productivity Commission Review of the contribution of the not-for-profit sector.

The BRCWG has also included regulatory reform of the third sector as part of its 2009 work plan.

Recommendation 8

The committee recommends that the Henry Review include an examination of taxation measures affecting not-for-profit organisations with a view to simplifying these arrangements and reducing confusion and cost of compliance for these organisations.

Commonwealth Government Response:

As part of the Henry Review, a discussion paper has been released to seek community input. Chapter 7 specifically relates to the tax treatment of not-for-profit organisations and possible alternative arrangements that may assist organisations to further their philanthropic and community-based activities.

Recommendation 9

The committee recommends that a National Fundraising Act be developed following a referral of powers from state and territories to the Commonwealth. This Act should include the following minimum features:

- a. It should apply nationally;
- b. It should apply to all organisations;
- c. It should require accounts or records to be submitted following the fundraising period with the level of reporting commensurate with the size of the organisation or amount raised; and
- d. It should include a provision for granting of a licence.
- e. It should clearly regulate contemporary fundraising activities such as Internet fundraising.

Commonwealth Government Response:

Noted. State and Territory Governments regulate fundraising activities in accordance with their own legislation. The BRCWG, as part of its 2009 work plan, is considering reform options to fundraising legislation.

Recommendation 10

The committee recommends that a tiered reporting system be established under the legislation for a specialist legal structure.

Recommendation 11

The committee recommends that the tiers be assigned to organisations based on total annual revenue.

Commonwealth Government Response to Recommendations 10 and 11:

Noted. Refer to response Recommendation 3.

The Treasury and policy reforms are being considered have conducted a review of financial reporting by unlisted companies under the *Corporations Act 2001* (Cth). The Commonwealth Government is also developing a Commonwealth grants policy framework that, amongst other things, will include arrangements to minimise unnecessary red tape for grant recipients.

Recommendation 12

The committee recommends that the Commonwealth Government with the Sector to implement a standard chart of accounts for use by all departments and not-for-profit organisations as a priority.

Recommendation 13

The committee recommends that a new disclosure regime contain elements of narrative and numeric reporting as well as financial, in acknowledgement that the stakeholders of the Sector want different information to that of shareholders in the Business Sector. The financial reporting should be transparent and facilitate comparison across charities.

Commonwealth Government Response to Recommendations 12 and 13:

Noted. The BRCWG, as part of its 2009 work plan, is considering reform options aimed at developing a standard chart of accounts.

The Commonwealth Government will also consider accounting disclosure regimes in light of the findings of the Review of financial reporting by unlisted companies by Treasury, which may address some of the issues raised by the Senate Committee.

The findings of the Review of accounting standards for 'Non-publicly Accountable Entities', that is non-listed entities, by the Australian Accounting Standards Board, and the Productivity Commission Review of the contribution of the not-for-profit sector will also be considered.

Recommendation 14

The committee recommends that the national regulator investigate the cost vs. benefits of a GuideStar-type system (a website portal that publishes information on the aims and activities of not-for-profit organisations) in Australia to encompass all not-for-profit organisations.

Commonwealth Government Response:

Noted. This recommendation will be considered within the context of the reviews noted. States and Territories will be consulted in the process.

Recommendation 15

The committee recommends that a Taskforce be established for the purpose of implementing the recommendations of this report. The Taskforce should report to COAG. Its membership should include:

- a. A government representative from the Commonwealth;
- b. A COAG-elected representative to speak for states and territories;
- c. One or more qualified legal experts with expertise with the major pieces of legislation affecting not-for-profit organisations;
- d. A representative from an organisation which manages private charitable foundations;
- e. An accountant with not-for-profit expertise; and
- f. A number of representatives from the peak bodies of not-for-profit organisations, including a representative from a peak body for social enterprises.

The Taskforce should actively seek to ensure that the measure of reform that it implements do not impose an unreasonable reporting burden on small and micro not-for-profit organisations.

Commonwealth Government Response:

Noted. The Commonwealth Government will consider the recommendations of the Senate Inquiry throughout 2009, as findings of various reviews are reported. It will consult extensively across the third sector, business community and State and Territory Governments and seek expert advice as required. The appropriate mechanism for consultation will be determined as the issues are considered.

APPENDIX 5:

Summary of the Productivity Commission's Recommendations

Recommendation 5.1

The Australian Government should initiate an Information Development Plan for the Not-for-profit sector. Given its central role in providing data on the sector and its legislated responsibility for formulating the Information Development Plan.

Recommendation 5.2

Australian governments should adopt a common framework for measuring the contribution of the not-for-profit sector. Having regard to the diversity of the sector's activities and structures, measurement using this framework should embody the principles of proportionality, transparency, robustness, flexibility, and relevance.

Recommendation 5.3

To minimise compliance costs and maximise the value of data collected, Australian governments should agree to implement a reform agenda for reporting and evaluation requirements for organisations involved in the delivery of government funded services. This should:

- commit to basing reporting and evaluation requirements in service delivery contracts on a common measurement framework (appropriately adapted to the specific circumstances of service delivery)
- require expenditure (input) measures to be based on the Standard Chart of Accounts
- develop data standards for the relevant non-expenditure items
- ensure that information generated through performance evaluations are returned to service providers to enable appropriate learning to take place and allow organisations to benchmark their performance
- employ, where practicable, the principle of 'report once, use often'.

Recommendation 5.4

The Australian Government should provide funding for the establishment of a Centre for Community Service Effectiveness to promote 'best practice' approaches to evaluation, with an initial focus on the evaluation of government funded community services. Over time, funding should also be sought from state/territory governments, business and from within the sector. Among its roles, the Centre should provide:

- a publicly available portal for lodging and accessing evaluations and related information provided by not-for-profit organisations and government agencies
- guidance for undertaking impact evaluations
- support for 'meta' analyses of evaluation results to be undertaken and made publicly available.

Recommendation 6.1

The Australian Government should amend the Corporations Act to establish a separate chapter relating to not-for-profit companies limited by guarantee. This should:

- embody the principles of proportionality in relation to reporting, fees and charges
- provide clear rules on the disposal of assets in the event of the company being dissolved or restructured, in addition to the proposed prohibition on the payment of dividends
- include a plain English guide (as currently exists for small and medium scale enterprises)

As part of this process, the Australian Government should, in consultation with stakeholders, examine whether there are additional requirements that are inappropriate or unduly restrictive for not-for-profit organisations that should also be addressed.

Recommendation 6.2

Australian governments should, through the Council of Australian Governments Business Regulation and Competition Working Group, pursue harmonisation of state and territory based incorporated associations legislation, with an initial focus on:

- aligning not-for-profit organisations' public corporate and financial reporting requirements
- rules on the distribution of assets on the dissolution or restructuring of a not-for-profit organisation
- allowing not-for-profit organisations to migrate from one legal form to another and to move to the Commonwealth jurisdiction without onerous transaction costs.

Recommendation 6.3

To promote confidence in and reduce the compliance costs associated with fundraising regulation, Australian governments, through the Council of Australian Governments Business Regulation and Competition Working Group, should:

- agree to and implement mutual recognition and harmonised fundraising regulation across Australia, through the establishment of model fundraising legislation
- support the development of a fundraising register for cross-jurisdictional fundraising organisations and/or activities, to be administered by the proposed national Registrar for Community and Charitable Purpose Organisations
- clarify the responsibility for regulation of fundraising undertaken through electronic media such as the internet, and move to ensure appropriate regulation of such mediums including through Commonwealth legislation.

Recommendation 6.4

Responsibility for endorsement for Commonwealth tax concessional status for not-for-profit organisations and maintaining a register of endorsed organisations should sit with the Registrar for Community and Charitable Purpose Organisations. To retain endorsement for Commonwealth tax concessions, endorsed organisations should be required to submit an annual community-purpose statement to the Registrar which would be accessible to the public. The

Australian Commissioner for Taxation should have the right to seek a review of decisions of the Registrar in relation to the endorsement of not-for-profit organisations for tax concessional status. The Commissioner should also have the power to issue a directive to the Registrar for the dis-endorsement of an organisation where there has been a breach of taxation compliance requirements.

Recommendation 6.5

The Australian Government should establish a one-stop-shop for Commonwealth regulation by consolidating various regulatory functions into a new national Registrar for Community and Charitable Purpose Organisations. While ultimately the Registrar could be an independent statutory body, initially it should be established as a statutory body corporate or organ in the Australian Securities and Investment Commission.

The Registrar will undertake the following key functions:

- register and regulate not-for-profit companies limited by guarantee and Indigenous corporations, with a stakeholder team dedicated to Indigenous corporations
- assess the eligibility of not-for-profit organisations for Commonwealth tax concession status endorsement and maintain a register of endorsed organisations
- register cross-jurisdictional fundraising organisations and/or activities by not-for-profit organisations
- provide a single reporting portal for public record corporate and financial information.
- provide appropriate guidance in relation to governance matters
- investigate compliance with regulatory requirements
- provide complaints handling in respect of the above functions.

Recommendation 6.6

The Registrar should implement the principle of ‘report once, use often’ by providing a single reporting portal and form for annual reporting on community- purpose, governance arrangements, financial accounts and fundraising activity. Australian governments, through the Council of Australian Governments, can support this principle and substantially reduce compliance costs for not-for-profit organisations by:

- adopting and developing an implementation strategy for the Standard Chart of Accounts for reporting by not-for-profits in receipt of government grants or service contracts
- expanding the Standard Business Reporting initiative to include reporting requirements by not-for-profits
- encouraging their agencies to utilise the governance and financial account information (that will be lodged with the Registrar) to meet their organisation level ‘health check’ requirements for contracting purposes.

Recommendation 7.1

The Australian Government should adopt a statutory definition of charitable purposes in accordance with the recommendations of the 2001 Inquiry into the Definition of Charities and Related Organisations.

Recommendation 7.2

State and territory governments should recognise the tax concession status endorsement of not-for-profit organisations at the Commonwealth level. Given the disparities between eligibility for tax concessions across jurisdictions, state and territory governments should utilise such Commonwealth endorsements in determining eligibility for their jurisdictional concessions, and seek to harmonise tax concessional status definitions or classifications with the Commonwealth over time.

Recommendation 7.3

The Australian Government should progressively widen the scope for gift deductibility to include all endorsed charitable institutions and charitable funds. Consistent with the Australian Taxation Office rulings on what constitutes a gift, payments for services should not qualify as a gift.

Recommendation 7.4

To encourage cost-effective giving, the Australian Government should explore options to promote and support planned giving, especially payroll giving. Specifically, the Australian Government should provide funding for a national campaign to promote payroll giving and the associated tax benefits. As part of the campaign, governments should encourage the establishment of payroll giving within all their agencies.

Recommendation 7.5

Australian governments should assist in the development of a sustainable market for not-for-profit organisations to access debt financing through:

- building business planning skills for not-for-profit organisations, notably social enterprises (recommendations 9.2 and 9.6)
- improving funding certainty for those not-for-profit organisations involved in the delivery of government services to improve loan viability by improving clarity about funding (recommendation 11.1) and the appropriate length of contract (recommendation 12.5)
- exploring options to encourage (for a limited period) community development financial institutions to develop appropriate financial products and services for the sector
- exploring options to make better use of the corpus of philanthropic foundations and trusts to make loans to deductible gift recipients and endorsed charitable institutions.

The Australian Government should establish an advisory panel, chaired by Treasury, to consider options and assess progress in developing a sustainable market for not-for-profit organisation debt products with the aim of establishing mainstream financial products for investors who are willing to accept a lower risk adjusted financial return for an accompanying social return.

Recommendation 8.1

The Department of the Treasury and Finance and Deregulation should jointly conduct a review into the feasibility, the costs and the benefits of requiring value for money assessments for governments' procurement to consider significant input tax concessions. Such a review should be wide-ranging, including the not-for-profit and for-profit sectors.

Recommendation 9.1

Information and communication technology has the potential to enable more cost-effective and higher quality human services. With due considerations to protocols for protecting privacy, in specific service areas, Australian governments should explore the potential for selective sharing of client information between agencies and not-for-profit organisations and other providers, through the utilisation of enhanced information and communication technology.

Recommendation 9.2

State and territory governments should review their full range of support for sector development to reduce duplication, improve the effectiveness of such measures, and strengthen strategic focus, including on:

- developing the sustainable use of intermediaries providing support services to the sector, including in information technology
- improving knowledge of, and the capacity to meet, the governance requirements for not-for-profit organisations' boards and management
- building skills in evaluation and risk management, with a priority for those not-for-profit organisations engaged in delivery of government funded services.

Recommendation 9.3

Australian government agencies providing extensive grants to, or using external agencies for, service delivery should establish evaluation programs to assess the effectiveness and actual cost of their programs. Where related to community services, these evaluations should be posted with the Centre for Community Service Effectiveness.

Recommendation 9.4

The Cooperative Research Centre program should facilitate applications by collaborations of not-for-profit organisations (include universities) government agencies and business in the areas of social innovation by:

- actively promoting the opportunities that are now available; and
- providing specialised advice and facilitation support to organisations expressing interest but lacking the knowledge and resources to develop the partnership required.

Recommendation 9.5

Australian governments should require all programs (of over \$10 million) delivering community services through not-for-profit organisations to set aside a small proportion of the program budget (for example, one per cent) to a

program related social innovation fund. The fund should support trials of new approaches to service delivery, including evaluation of their cost-effectiveness.

Recommendation 9.6

The Australian Government should fund the Enterprise Connect program to expand its specialised services to a new Centre that provides business advisory services to organisations involved in social enterprise activity.

Recommendation 10.1

Australian governments should introduce a system of 'Working with Vulnerable People Checks' that provides for checks to be portable between organisations for a designated time period.

Further, Australian governments should explore the feasibility of developing a consistent national system allowing portability across states and territories of police checks and the exchange of information on people deemed unsuitable for working with vulnerable people, especially children.

Recommendation 10.2

In order to ensure that not-for-profits can sustain their workforces, and as wages are a major factor in the successful recruitment and retention of staff, Australian governments purchasing community services need to base funding on relevant market wages for equivalent positions. Costings need to take into account the skill sets required to perform the purchased services and be indexed appropriately to market wage growth within that industry sector.

Recommendation 10.3

The Australian Government, in consultation with Skills Australia, should commission the Community Services and Health Industry Skills Council to undertake workforce planning for the community services sector having regard to the current and future workforce challenges arising from growing demand and increasing supply constraints.

Recommendation 11.1

Australian governments should, in the contracting of services or other funding of external organisations, determine and transparently articulate whether they are fully funding particular services or activities undertaken by not-for-profit organisations, or only making a contribution towards the associated costs and the extent of that contribution. Australian governments should fully fund those services that they would otherwise provide directly (allowing for co-contributions from clients and any agreed contributions by service providers). In applying this criterion, governments should have regard to whether the funded activity is considered essential, as part of the social safety net or an entitlement for eligible Australians.

Recommendation 11.2

Australian governments should ensure that service agreements and contracts include provision for reasonable compensation for providers for the costs imposed by changes in government policy that affect the delivery of the

contracted service, for example, changes to eligibility rules, the scope of the service being provided, or reporting requirements.

Australian governments funding service provision or making grants should respect the independence of funded organisations and not impose conditions associated with the general operations of the funded organisation, beyond those essential to ensure the delivery of agreed funding outcomes.

Recommendation 12.1

Australian governments should ensure that they choose the model of engagement with not-for-profits that best suits the characteristics and circumstances of the service being delivered. In choosing between alternative models of engagement, governments should consider the nature of the outcomes sought, the characteristics of clients, and the nature of the market. In particular:

- there should be no presumption that purchase of service contracting will always be the most appropriate model;
- where governments are seeking the delivery of a clearly defined outcome and markets are genuinely contestable purchase of service contracting should remain the preferred approach; and
- where truly competitive markets develop and clients face real choice in the services available to them, governments should consider moving to client-directed service delivery models. This transition should be conditional upon there being appropriate safeguards in place to protect and empower vulnerable clients (or their carers) in exercising choice and ensure an acceptable minimum level of service quality and provision.

Recommendation 12.2

Where a market-based approach is not feasible or appropriate, governments should use other models of engagement. This may involve governments entering into either extended life or short-term joint ventures.

Extended life joint ventures should adopt an iterative process that will:

- involve all parties in the design of the program;
- embed and fund an agreed evaluation process, informing program design and modification;
- regularly review and revise the service delivery approaches in light of findings from evaluation, changing demands or environmental conditions; and
- provide long-term or rolling funding with capacity to adjust funding in light of the modifications.

Recommendation 12.3

Australian governments should ensure that whatever model of engagement is used to underpin the delivery of services it is consistent with the overarching principle of obtaining the best value for money for the community. In determining value for money, governments should explicitly recognise any indirect or wider benefits that providers may be able to generate. An evidence based approach should be used to assess the nature, extent and relevance of these types of benefits on a case-by-case basis.

Recommendation 12.4

Australian governments should assess the relative merits of the lead agency model on a case-by-case basis. This should include an assessment of the costs to not-for-profits of adopting this approach including any duplication of reporting and accountability requirements, the additional transaction costs associated with sub-contracting, and the potential for loss of diversity among providers.

Recommendation 12.5

The length of service agreements and contracts should reflect the length of the period required to achieve agreed outcomes rather than having arbitrary or standard contract periods. Extended life service agreements or contracts should set out clearly established:

- processes for periodically reviewing progress towards achieving a program's objectives; and
- conditions under which a service may be opened up to new service providers or a provider's involvement is scaled back or terminated.

Recommendation 12.6

When entering into service agreements and contracts for the delivery of services, government agencies should develop an explicit risk management framework in consultation with providers and through the use of appropriately trained staff. This should include:

- allocating risk to the party best able to bear the risk
- establishing agreed protocols for managing risk over the life of the contract.

Recommendation 12.7

Australian governments should urgently review and streamline their tendering, contracting, reporting and acquittal requirements in the provision of services to reduce compliance costs. This should seek to ensure that the compliance burden associated with these requirements is proportionate to the funding provided and risk involved.

Further, to reduce the current need to verify the provider's corporate or financial health on multiple occasions, even within the same agency, reviews should include consideration of:

- development of Master Agreements that are fit-for-purpose, at least at a whole-of-agency level; and
- use of pre-qualifying panels of service providers.

Recommendation 12.8

The Department of Finance and Deregulation should develop a common set of core principles to underpin all government service agreements and contracts in the human services area. This should be done in consultation with relevant government departments and agencies and service providers.

Recommendation 14.1

The Australian Government should establish an Office for Not-For-Profit Sector Engagement, for an initial term of five years. The Office would support the Australian Government in its efforts to:

- implement sector regulatory and other reforms and the implementation of the Government's proposed compact with the not-for-profit sector;
- promote the development and implementation of the proposed Information Development Plan;
- oversee the establishment of the proposed Centre for Community Service Effectiveness;
- implement the proposed contracting reforms in government funded services
- act as a catalyst for the promotion and funding by government agencies of social innovation programs
- facilitate the establishment of the advisory panel on development of a not-for-profit capital market; and
- facilitate stronger community and business collaboration. The Office should, through the relevant Minister, report publicly on an annual basis on its achievements.

Recommendation 14.2

Compacts between Australian governments and the sector must be supported by well documented plans of action, including at agency level, if appropriate, and supported by practical measures including monitoring and evaluative processes that give concrete expression to the proposed relationship.

Recommendation 14.3

State and territory governments should develop a public strategy for implementing government-sector reforms arising from this report. Priority areas should include means to improve government-sector engagement, enhanced risk assessment and risk management strategies, contract design, effective reporting, and evaluation methods.

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